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Business this week

Jun 7th 2001
From The Economist print edition

Steel resolve

George Bush announced that America would investigate unfair trade practices in the **global steel industry** with the intent of imposing new anti-dumping duties.

See article: George Bush's new plan for the steel industry

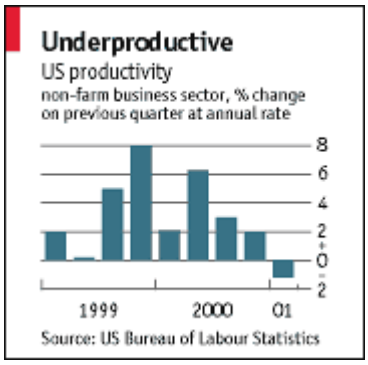
In response to the United Nations Security Council's decision on sanctions, **Iraq** cut off its oil exports of about 2.1m barrels a day. Saudi Arabia said it would make up the difference.

See article: OPEC needs to keep Iraq from destabilising the world's oil market

Economy measures

Consumer confidence in the **euro area** fell more heavily than expected in May, after a fall of business confidence had suggested that, although Europe's economy has weathered the global downturn better than most, it is now slowing. But euro-area unemployment fell slightly in April, to 8.3%.

The productivity of workers in the **United States** fell in the first quarter by 1.2% at an annual rate, according to revised figures. This is the first time that labour productivity has fallen since 1995.



In an effort to stave off fears of a debt default and to buy time for the country's economy to pull out of a three-year recession, **Argentina** announced that it had swapped $29.5 billion of bonds falling due before 2005 for new, longer-dated bonds.

See article: Argentina's bond swap buys time at a high price

Legal matters

A jury in California ordered **Philip Morris** to pay damages of $3 billion for a smoker with lung cancer—by far the biggest such award against a tobacco company. Philip Morris will appeal.

See article: Another blow against Big Tobacco

Flight details

Orbitz, an online travel agency set up by five American airlines, was launched with a bang, and promptly went down after being deluged by customers. United, American, Delta, Continental and Northwest expect to take a chunk of business from their two main rivals, Expedia and Travelocity.

America's **Federal Aviation Administration** outlined a ten-year plan to overhaul the country's airline industry. Greater passenger capacity, more runways and new routes will be introduced to reduce delays and improve safety.

See article: How to improve America's airtraffic control

General Electric is poised to sell Honeywell International's regional jet-engine business in an effort to persuade the European Commission to approve GE's $40 billion bid for Honeywell.

Shares in **Railtrack**, operators of Britain's rail network, dipped 17% in one day as the beleaguered company was due to drop out of Britain's FTSE 100 share index. It will be replaced in the index by Next, a purveyor of mid-market clothing.

See article: More trouble for Railtrack

Swiss bank accounts

Moody's, a credit-rating agency, downgraded **UBS**, after the Swiss bank had failed to make big advances in onshore private banking for the world's very rich. Domestic banks have grabbed much of this business in their own countries.

CSFB was deemed to have broken New Zealand stock-exchange rules in a takeover scrap for Montana, a big winemaker. Indian regulators have also banned it from stockbroking after a price-fixing investigation. Its now defunct Japanese derivatives business broke securities laws and, in America, it is undergoing investigations linked to rigged initial public offerings.

Business in Europe

After 12 years of tortuous negotiation, the European Union at last reached a provisional agreement on a **takeover directive**. The directive still has to be formally approved, however, and the European Parliament may yet decide to block it.

See article: The EU takeover directive may yet pass

Germany's telecoms regulator ruled that companies that have acquired the six third-generation mobile-phone licences will be able to share the costs of building new infrastructure. The money- saving scheme is likely to be challenged by Vodafone and Deutsche Telekom, both incumbents with upgradable networks already in place.

See article: Sharing 3G networks

Cadbury Schweppes, a British drinks firm, said it was close to an agreement to buy **Orangina**, a soft-drinks company, from **Pernod Ricard**, a French counterpart, for *euro*700m ($826m).

EPA

Italy's government called on **EDF**, a French power giant, to reduce its recently acquired 20% stake in **Montedison**, Italy's largest power company, to under 2%. Italy objects to EDF's involvement in its newly opened power markets because France has been slow to deregulate its own market. EDF said "non".

Saudi Arabia's government signed three deals worth $25 billion to develop natural gas reserves, two headed by ExxonMobil and one by Royal Dutch/Shell. The Saudis hope that the use of foreign private capital will help to revive the kingdom's state-dominated economy which has not grown fast enough.

See article: Investment in Saudi Arabia

Martin Ebner's BZ Group took a 10% voting stake in Investor, a Swedish holding company controlled by the Wallenberg family. Mr Ebner wants a share buyback, spin-offs and a loosening of the grip of the Wallenbergs on the company.

See article: Ebner v the Wallenbergs

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Politics this week

Jun 7th 2001
From The Economist print edition

Ceasefire at last?

A Palestinian **suicide-bomber** killed 20 Israeli youngsters at a Tel Aviv discotheque. Israel held back from massive retaliation after Yasser Arafat committed his forces to an unconditional ceasefire. George Tenet, the CIA's director, arrived to help promote this tentative pause in the violence, but a Hamas spokesman denied that there was a ceasefire.

See article: A fragile Israeli-Palestinian ceasefire

AP

The king of **Nepal** and nine other members of the royal family were shot dead, apparently by the crown prince, Dipendra. He later died from self-inflicted wounds. Curfews were introduced in the capital, Katmandu, after riots by Nepalis confused by contradictory stories and demanding the truth about the killings.

See article: After the palace massacre in Nepal

Makiko Tanaka, **Japan**'s outspoken foreign minister, embarrassed her government by expressing doubts about President George Bush's missile-defence plans.

Voters decide

Voters in **Britain** went to the polls in a general election, which Tony Blair's Labour Party looked likely to win easily. Harder questions: would William Hague survive as leader of the opposition Tory party? And would Mr Blair call a referendum on the euro next year?

See article: Labour's second term

Alejandro Toledo, an economist of Andean Indian descent, was elected president of **Peru**, narrowly defeating Alan Garcia, a populist former president.

AP

See article: The tasks awaiting Alejandro Toledo

Ireland held a referendum on the European Union's Nice treaty, with the once-confident Yes side still expecting victory but worried by a sudden rise in support for No in the opinion polls.

Silvio Berlusconi was formally invited by Italy's president to form its new government.

In the unrecognised but rather successful state of **Somaliland**, a huge majority voted in favour of independence from the rest of Somalia.

James Hahn, the city attorney, won a run-off to become the new mayor of **Los Angeles**, beating his fellow Democrat, Antonio Villaraigosa, who had hoped to be the city's first Latino mayor since 1872.

See article: A new mayor for Los Angeles

Haiti's president, Jean-Bertrand Aristide, agreed to hold new parliamentary elections. In return, the Organisation of American States said it would help Haiti obtain $500m of suspended aid.

Democrats officially took control of the United States **Senate** for the first time in six years. The Democratic leader, Tom Daschle, promised to adopt a co-operative approach towards the Republican agenda.

War and peace

Fighting continued in Bangui, the capital of the **Central African Republic**, after last week's failed coup against President Ange-Félix Patassé.

See article: The Central African Republic erupts

In **Colombia**, the FARC guerrillas and the government began an exchange of sick prisoners, the first practical result of more than two years of peace talks.

See article: A modest peace deal in Colombia

Prime Minister Ljubco Georgievski again threatened to declare a formal state of war in **Macedonia** after ethnic-Albanian rebels, seeking to widen the conflict to an area hitherto unaffected, killed five government soldiers north-west of Skopje, the capital.

Visiting Europe, America's defence secretary, Donald Rumsfeld, reassured NATO allies that no hasty reduction of American forces was planned in the Balkans. President Bush said that America would reopen talks with **North Korea**, broken off three months ago, to discuss missiles, nuclear concerns and conventional forces.

See article: Difficult times in America's relations with Europe

A deal seemed near to overcoming Turkish objections to NATO co-operation with the **European Union**'s rapid-reaction force**.**

Nine of the 20 hostages held by Muslim rebels in the **Philippines** escaped after fighting between their Abu Sayyaf captors and Philippine troops.

Chenjerai Hunzvi, the leader of **Zimbabwe**'s "war veterans", died of malaria. Calling himself Hitler, he had led violent attacks on Robert Mugabe's opponents and encouraged the occupation of white-owned farms. Mr Mugabe declared him a national hero.

Legal matters

France's prime minister, **Lionel Jospin**, admitted that he had belonged to a Trotskyite organisation—a fact he had previously denied.

AP

See article: France's prime minister has a past

President Vojislav Kostunica of Yugoslavia appealed to his allies in a Montenegrin party not to block a draft law that would allow ex-President **Slobodan Milosevic** to be extradited to The Hague for war crimes.

See article: Serbia and Slobodan Milosevic's fate

An American federal judge ruled that the execution to **Timothy McVeigh**, the convicted Oklahoma City bomber, would go ahead on June 11th. Lawyers for Mr McVeigh had argued that they needed more time to look at documents withheld by the FBI during the trial.

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Europe and America

Mr Bush goes to Europe

Jun 7th 2001
From The Economist print edition

For all their squabbles, America and Europe are not alien worlds. They still have lots in common

AP

WHEN George Bush arrives in Europe next week, he will find not quite a lunar landscape but a political one littered with disputes (see article). He will also find many Europeans apparently inclined to believe that he is uninterested in co-operation, perhaps because so many voices in his own administration seem inclined to believe that America should do its own thing in its own way, never mind the rest of the world, including the have-your-cake-and-eat-it Europeans. Inevitably, some will speculate that this is the end of an affair that dates back, with breaks, at least to 1917, and culminated in marital alliance with the signing of the NATO pact in 1949.

The Euro-American relationship does indeed have something in common with a marriage, but countries are not people: they pursue interests, not affairs of the heart. If the alliance is to fall apart, it will be either because America's interests cease to be congruent with Europe's, or because the two sides carelessly allow their friendship to fall into disrepair. Fortunately, neither of those developments has yet come to pass. As so often in Euro-American relations, appearances deceive.

Disputation is the stuff of alliances, marital or otherwise, and the ether above the Atlantic has often crackled angrily over trade disputes, Suez adventures, missile deployments and so on. In time, with luck and good management, the squabbles that now separate the allies will go the way of these past rows, all of which gave rise to dark forebodings. But a happy outcome is not inevitable. It depends on a common, and correct, appreciation both of what is happening and of what is genuinely at stake in the transatlantic alliance.

Go-it-alone America

The arrival of Mr Bush in the White House seems to represent a clear break with the past. In truth it merely brings into focus the fact that America's furrow in world affairs has long been diverging from the European Union's. Mr Bush has appointed a host of officials who reject multilateralism—or at least many United Nations activities, treaties on global warming, nuclear tests and a world criminal court, or joint action on tax havens. Whether these officials will prevail is still unclear. Their unilateralist tendencies, however, have long been present, especially in Congress, which had put 70 countries under sanctions by 1999, balked at paying America's UN dues and thumbed its nose at the Kyoto climate-change treaty long before Mr Bush, too, gave it a Bronx cheer. The Senate, indeed, had refused to ratify more than 60 treaties negotiated by the United States. And therein lies a clue to the new danger: that this administration might reinforce the unilateralism of Congress, whereas its predecessors, Republican and Democratic alike, have generally resisted it.

The danger in Europe is different: it is that it meets what it sees as American arrogance with an arrogance of its own, deluding itself that it can have superpower status without political maturity and defence spending to match, and creating institutions (its rapid-reaction force?) to compete with America rather than to complement NATO. Here too the tendencies have been evident for a while, though they are not, at present, in the ascendant. Europeans can be hypocritical—not one EU government has yet ratified the Kyoto treaty—but most know their collective foreign-policy prowess is modest. And their new defence force, boosted this week by a deal-in-the-making with Turkey, should in time fit in harmoniously with NATO.

So a transatlantic bust-up is not imminent. But it will remain a possibility. The United States is a very different place from Europe, and the differences will grow. Demographically, Americans are increasingly Asian and Latino, less inclined when looking “home” to turn to Europe. Their affection for guns, religion, the death penalty and genetically modified crops seems strange to Europeans. Just as baffling to Americans is Europeans’ toleration of high taxes, fussy regulation and indulgent state help for idlers and unfortunates. While Americans remain individualistic citizens of a nation-state at the height of its power, Europeans are absorbed in an unprecedented enterprise of union-building. Good luck to them, Americans may say. Let them sort out their Balkan backyard.

The ties that bind

Yet these two partners still have much in common. They are, together, not only the main engine of the world’s economy but the main custodian of its liberal values. They have strong interests in common, and each has additional interests in persuading the other to be at least partly involved in less obvious areas of concern: America needs European help in Asia, Europe needs American help almost everywhere. Why? Because neither power, not even the United States, is usually strong enough, on its own, to carry the day. Moreover, experience—remember Bosnia—shows that one without the other makes little headway, whereas the two together can be effective.

Solutions exist, or can be found, for all the problems that beset the allies, so long as they are prepared to work to settle their differences. The Europeans will swallow their reservations about missile defences, if Mr Bush can persuade them that the pursuit is practical (and practicable), not ideological; a deal can surely be done with the Russians over the Anti-Ballistic Missile Treaty. For their part, the Americans will swallow their reservations about Europe’s defence initiative, if it does not draw resources away from NATO. The settlement of the long-running banana dispute shows that trade rows need not be terminal. Even apparently jarringly different policies—as over the Middle East or North Korea—can in practice be combined to promote a common objective.

First, however, the two sides must realise how much they need each other. Europe would soon discover the truth of that if Mr Bush were to pull his forces out of the Balkans (better take them from Germany first). America might take longer to feel Europe’s absence, but it would only be a matter of time. They may have no common Soviet enemy, but they still have common values, and a common interest in upholding them. In an alliance based on interests, not wedlock, that should be enough to keep Europe and America together for a while.

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After Peru's election

A test of Toledo's steel

Jun 7th 2001
From The Economist print edition

The new president has much to do to overcome the legacies of authoritarianism

Reuters

IT WAS fitting that Alejandro Toledo should win the run-off ballot for Peru's presidency on June 3rd. Many of his countrymen believe that only fraud and manipulation denied him victory last year, when he challenged Alberto Fujimori. Now, at last, after four elections and 18 months of political turmoil and economic stagnation, Peru has the chance not just to close an extraordinary and damaging chapter in its history, but to rebuild its democracy.

Mr Toledo won by only five percentage points over Alan Garcia, an incompetent ex-president who has now achieved an improbable political rehabilitation. Nevertheless, the voters' decision to reject Mr Garcia's insidious populism sent a clear message. They preferred Mr Toledo despite his flaws—exposed both by relentless campaigning and by the attentions of Mr Fujimori's intelligence service. There are doubts about Mr Toledo's honesty in personal matters, lurid claims about incidents in his private life, an impulsive temperament and an evident intoxication with the crowd. But Mr Toledo's blemishes are minor compared with those of Mr Garcia, or for that matter Mr Fujimori. He deserves the benefit of the doubt.

Mr Toledo earns respect not just for his tireless campaign against Mr Fujimori's authoritarian regime, but also for his lifelong struggle against adversity. One of a family of 16 children who worked briefly as a shoeshine boy before winning a scholarship that led to a Stanford doctorate, he is Peru's first democratically-elected president of Andean Indian descent.

That is important, although its significance has been misinterpreted. His supporters, including his Belgian-born wife, have fancifully portrayed Mr Toledo as a latter-day Inca. He is not. Neither does he represent any organised Indian movement of the kind that exists in Ecuador, Mexico or even Bolivia. Rather, he embodies social mobility in a still-stratified society—and thus a justified demand that Peru should do much more to offer equal opportunities to its people of indigenous descent, who suffer disproportionately from poverty, deprivation and political impotence.

The tasks facing Mr Toledo are huge (see article). Peru's public institutions were subverted and its political morality debauched by Mr Fujimori. His closest adviser, Vladimiro Montesinos, used bribery and corruption on an extraordinarily systematic scale to control and manipulate the judiciary, Congress, the media and even private business. What made all this harder to stomach for many Peruvians was that they had once had such high hopes of Mr Fujimori.

So the first job for Mr Toledo is to restore Peruvians' battered confidence in democratic politics. A good start has been made by the caretaker government that took over after Mr Fujimori fled to Japan in November. The next step is for Mr Toledo to seek a broad consensus for reforms. Mr Fujimori liked to keep all power in his own hands—or, as it turned out, those of Mr Montesinos and the army. Now Peru needs the rule of law, some decentralisation of power, a less political army and independent institutions to keep the executive honest.

If crime by those in power is to be seen not to pay, Mr Fujimori, Mr Montesinos and their cronies must be brought to book. That is something with which outsiders could help. Japan has been over-generous to Mr Fujimori in accepting his claim of Japanese nationality; Venezuela would appear to be sheltering Mr Montesinos; and the United States has been unforthcoming about its close relationship over a decade with the former intelligence chief.

The second urgent job is to rouse the economy from paralysis induced by political uncertainty. Mr Toledo, who has promised market-friendly policies, can call on some capable advisers. Their task will be to bring back the high growth rates of Mr Fujimori's best years, while spreading wide the benefits of that expansion. That will require a huge effort to improve education—while resisting the temptation to seek ephemeral popularity with unaffordable subsidies for job-creation.

To do all this, Mr Toledo can count only on much goodwill at home and abroad, a loose political movement and, with luck, a narrow congressional majority thanks to some shaky alliances. That may be enough if things go well. But it is not hard to see how Peru, with a frustrated populace, a large illegal drug industry and some vestigial terrorist bands, could once again become difficult to govern, as several of its Andean neighbours already are. Economic growth and strong democratic government can be mutually reinforcing—but the lack of either debilitates the other. Mr Toledo has at last won a long battle—but a harder one now begins.

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Energy prices

When caps do not fit

Jun 7th 2001
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Controls on energy prices sound appealing to consumers, but they are wrong-headed

PRICE controls in the United States of America? Three decades after Richard Nixon's failed experiment with fixing wages and prices, and his even more foolish controls on oil prices, the idea seems unimaginable. Yet a growing chorus of Americans is now advocating price controls on gasoline, natural gas and, most of all, electricity.

This chorus has included, notably, populist Californian politicians, ensnared by the state's prolonged electricity troubles. Rather than fixing the botched deregulation that created those troubles, these politicians have been baying for the federal government to match the state's retail-price controls with caps on wholesale prices for electricity. President Bush has resisted demands that the Federal Energy Regulatory Commission (FERC), which oversees the interstate electricity market, should impose such caps—a stance he firmly repeated to California's governor, Gray Davis, last week.

But the president's principled stand against price controls may prove trickier to sustain in the days ahead. The shift in control of the Senate to the Democrats has bolstered the power of those who like price controls. Carl Levin of Michigan, who wants to launch a probe of retail gasoline prices, accuses oil companies of gouging consumers, pointing to their recent record profits. This has led to talk of setting ceilings on gasoline prices. The new Senate may also revive legislation to force the FERC to impose controls on electricity prices in California and other western states. The Senate's energy committee is no longer headed by Alaska's Frank Murkowski, a foe of price caps, but by New Mexico's Jeff Bingaman, who promises to make price caps a priority. So does Vice-President Al Gore's former running mate, Joseph Lieberman of Connecticut.

Emboldened by new support within the Senate, Mr Davis has responded to the president's refusal to intervene by threatening to sue the FERC to force it to impose price caps (although a federal court has just thrown out a similar case). Price controls clearly chime with public sentiment, too: a poll this week found that 56% of Americans favour price caps for energy.

That makes it worthwhile to repeat the lesson from past experience: price caps are a folly. When introduced in tight commodity markets, they only make things worse. In energy, they would weaken the incentives for consumers towards conservation. And they would discourage suppliers from making investments in power plants and the like that would ultimately relieve shortages. Indeed, price controls have often led to forced rationing through queues or power cuts. From California to Brazil (which has also just bungled its way into an electricity crisis), retail-price controls imposed to protect consumers have been a main contributor to the ills that consumers now rail against. It is idiotic to treat a self-inflicted illness by inflicting more of the same.

Awkward things, markets

To be fair, two rather more sophisticated arguments are put forward for energy-price controls. One is that most energy markets are not genuinely competitive, thanks to collusion and other illegal behaviour by energy producers and sellers. That is indeed a grave concern. However, price caps are not the remedy. If those hurling accusations of "price gouging" have any evidence of wrongdoing, they should have resort to America's strong competition and antitrust laws, rather than to meddling even more with the market.

The second argument is that temporary price caps, set at a level that allows “reasonable” profits, may be a necessary part of a broader reform of flawed markets. California’s power market certainly needs fixing. But allowing politicians rather than competition to dictate “reasonable” profits is a sure formula for disaster. And “temporary” price caps have a funny way of turning out to be not so temporary.

Even if those objections are overlooked, and price caps imposed as an unpalatable if necessary interim measure, one inconvenient fact remains. None of those arguing for price controls, whether on gasoline, natural gas or electricity, has proposed credible fixes for the structural defects that pushed prices up in the first place. Price caps should, in short, be seen for what they are: part of the problem, not the solution.

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And now for Europe?

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From The Economist print edition

Europe is at the top of Tony Blair's agenda, but he should not rush into a referendum on euro entry

TONY BLAIR has done what no other British politician has ever done: he has persuaded the British electorate to give the Labour Party two full terms in power. As the opinion polls predicted, Mr Blair won another big majority. And his opponent, William Hague, promptly announced his resignation.

Mr Blair will need his big majority. The tasks that face him in his second term (see article) are more difficult than those that faced him in his first four years. Last time around, he had to transform the Labour Party, to persuade voters that it could be trusted with the economy. This time, he has set himself the job of transforming the British state (by reforming the country's underperforming public services) and its relationship with the rest of the world (by offering voters a referendum on whether or not Britain should join Europe's single currency).

Mr Blair, it is generally believed, wants to join the euro. He is a European sort of chap. He holidays in Tuscany, not Florida. He speaks decent French. He wants to put Britain "at the heart of Europe". He dreams of Britain emulating the higher standard of public services enjoyed by Europe's richer countries.

But most British voters do not share Mr Blair's tastes. For a whole complex of reasons to do with the natural scratchiness of neighbours, fascism, communism and bad experiences in Parisian cafés, most people are hostile not just to the idea of "ever closer union" that is embedded in the European Union's founding Treaty of Rome, but also to its most tangible expression, membership of the European single currency. Around 70% of Britons say they do not want to join the euro.

Even for a man with Mr Blair's considerable powers of persuasion, that is a big number to shift. The 1975 referendum on whether Britain should pull out of the European Economic Community is often cited as encouragement for him, because a majority wanted to pull out at the beginning of the campaign, and the referendum endorsed staying in. But the Europhiles had an easier task, then. In 1975, all the big political parties, newspapers and lobby groups were on their side. This time, many have joined the antis.

Don't go yet

Mr Blair has not set a date for a referendum. He has said that Britain must first meet five economic conditions, but they are pretty subjective, so most people think he will go when he thinks he can win. His problem is that he does not know whether he can persuade people to vote for entry until he has started to campaign for it, and he cannot campaign for it properly without committing himself to a vote that he may lose.

Mr Blair's European counterparts want him to get on with it because they are fed up with Britain's ambivalence. The Conservative Party wants him to get on with it because it reckons the antis can win. The Liberal Democrats want him to get on with it because they reckon the pros can win. The newspapers want him to get on with it because it will be a good story. *The Economist*, which is happy in principle for Britain to join the euro, does not want him to get on with it. Here's why.

The economic case for going soon depends on the idea that postponing the decision would have as bad an effect as saying no. Companies looking to invest will favour countries within the eurozone, say those who want a referendum soon, because of the greater exchange-rate stability and lower transaction costs it offers; so the eurozone will attract more investment, and more investment means more jobs. If Britain

puts off a decision, investment will slip away.

Yet the facts do not, so far, support that view. For most of the past decade Germany and France have been working on the single currency, while Britain has become increasingly detached from the idea, all with no visible effect on the pattern of foreign direct investment. In the second half of the 1990s, the flow of FDI rose from $24 billion a year to $39 billion a year in France, from $12 billion to $27 billion in Germany and from $20 billion to $82 billion in Britain.

There's plenty to do at home

The political case for getting on with it is that Britain has influence in Brussels because its partners assume that euro entry is imminent; and that as the prospect of British entry fades, so will Britain's voice. But that is a case which Mr Blair will find hard to argue in a referendum, since he told the *Times*, "We absolutely have not and do not need to be a member to make our position strongly felt." Anyway, influence is determined largely by power, and Britain's power in Europe is institutionalised through, for instance, its voting weight in the Council of Ministers and its veto over certain policy areas. Membership of the single currency does not affect that.

The political arguments, it seems to us, tip the balance in the opposite direction. Europe is currently engaged in a wide-ranging debate about the future of the union leading up to the inter-governmental conference in 2004. Until those arguments are resolved it remains unclear whether the EU will expand its powers over taxation and social legislation; whether power will shift to the Council of Ministers, to a strengthened commission or to the European Parliament; whether there will be some body charged with "economic government" as a counterweight to the European Central Bank; what force the Charter of Fundamental Rights agreed at the Nice summit will have. And until those issues are resolved, it would be unwise to deepen Britain's relationship with the EU—and it will be a lot harder to persuade British voters to say yes to the euro.

Mr Blair might well think differently. His victory this week may make him believe he can afford the risk of losing a referendum. And the approaching 2004 conference may tempt him to think that if he loses a referendum in 2002 he could have another go in 2005 or 2006, at which point joining could look both safe and inevitable.

But this is to gamble with history for the sake of political tactics. Mr Blair would do Britain, and himself, a favour, if he were to postpone the idea of a referendum until it is clearer what sort of union Europe is turning into. For the moment, he should concentrate on improving Britain's public services. That will keep him busy enough.

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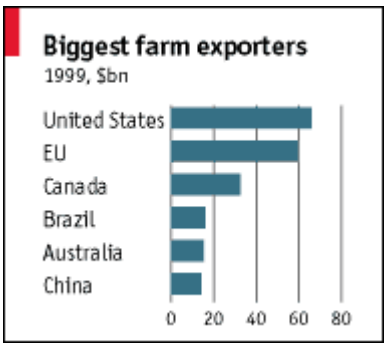
Agricultural subsidies

Towards efficient farm support

Jun 7th 2001
From The Economist print edition

It is time to replace indiscriminate subsidies to agriculture with a new mechanism



THE World Trade Organisation is girding itself up to launch a round of trade talks in November. Despite failing to agree a deal with America this week, China still hopes to seal its WTO membership later this month. Both developments make the time ripe for dealing with perhaps the biggest blot on the world's trading system: agriculture. Interference in agricultural markets remains endemic, even as big countries struggle to fulfil their commitments from the previous set of trade talks, the Uruguay Round (see article). Early negotiations hint at progress on the most egregious trade distortions. Domestic support, however, is harder to tackle.

All of the WTO's 141 members have a stake in farm trade, and most hold their positions passionately. The politics of farming have been sensitive at least since this newspaper campaigned against Britain's Corn Laws in the 1840s; it is no surprise that agriculture has lagged behind in trade liberalisation. This time around, too, the WTO's talks coincide with the formulation of a new, five-year farm bill in America and with growing arguments over the reform of the European Union's Common Agricultural Policy ahead of enlargement.

Most support measures offered by governments—payments to farmers, price subsidies, intervention purchases and so on—are justified by appealing to broader social benefits. These are said to include environmental protection, food security, sustaining poor rural communities and the preservation of cultural traditions. Yet most such benefits could be achieved more directly and at lower cost. To protect the environment, for instance, governments could set aside nature reserves; to sustain rural communities, they could use redistributive taxation; to enhance food security, they could buy up stockpiles on world markets.

Other benefits, such as the preservation of rural traditions and the satisfaction of having farms to look at, cannot be derived from anything other than local, non-intensive farming. But these benefits are not factored into farm prices. Left to its own devices, therefore, the market will not deliver enough non-intensively farmed acres. The economics of externalities argue for enhancing this type of farming so as to maximise society's well-being. That, in essence, is the case for public support for farmers. But even on this basis the way that governments have chosen to deliver it distorts prices, trade and behaviour, at huge cost.

Better targeting

A sounder system would aim directly at what is desired. If governments want to increase non-intensive farming, they should rely on those farmers most able to practise it. One way to do this would be to impose tradeable "obligations" that demand non-intensively farmed acres, somewhat analogous to pollution permits. Each year, governments would decide how many non-intensive acres they wanted. They would then allot obligations, which producers could trade.

A scheme like this would have several advantages. First, it would be economically efficient: farmers who benefit most from intensive farming would trade their obligations with those who can run non-intensive farming at least cost. The distribution of obligations could be skewed towards smaller or poorer farmers, if desired. Big, intensive farms would also pay the less well-off to take on their obligations; that would help to sustain farm-reliant communities.

A system like this would also be completely transparent. Monitoring should be feasible: at a crop-by-crop level, checking how many acres are farmed non-intensively requires only information on acreage and the

volume of production, plus occasional inspections. The system would be easily adaptable to changing economic and environmental conditions. A different target for non-intensive acreage could be set each year. And the whole plan would cost governments far less than farm support does today.

Best of all, this system would distort trade as little as possible. It would change the composition of farms, but not necessarily their production; one would expect many intensively farmed acres to be replaced by non-intensive acres. This may result in slightly higher prices, but only to the extent that non-intensive farming carries social benefits; so society would be better off. The key would be to find out whether these benefits really exist. To do that, governments would have to assess how much their people really value having non-intensive farms. That would give an idea of how much support is enhancing social welfare, rather than merely distorting markets.

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American justice

Free Jenna!

Jun 7th 2001
From The Economist print edition

A Joan of Arc, burning on the pyre of American puritanism

Reuters

FORGET about the Senate or Californian black-outs. This summer, there is only one story in America: the attempt by two 19-year-old girls, the president's daughters as it happens, to buy drinks in a Mexican restaurant in Austin, Texas. This was Jenna Bush's second alcohol-related offence in just over a month in a state that imposes mandatory prison sentences for a third offence. She compounded her crime by using a fake ID to try to buy her margarita—and by encouraging her goody-two-shoes twin sister, Barbara, to join her in flouting the law.

"Margaritagate" has launched a national debate about everything from journalistic ethics to teenage stress syndrome. Some of the ghastly "doctors" who take over TV screens at moments like these have even blamed George Bush (he gave up drinking through cold turkey, rather than encouraging his entire family to "work through" his drinking problems with him). But there has been no national debate on the one subject that is crying out for reconsideration: America's absurd insistence that people cannot drink until the age of 21. Most other countries allow people to buy alcohol at the age of 18. Americans can marry, breed, abort their unborn children, pay taxes, appear in pornographic films, fight for their country and even vote at that age. But buy a margarita with your Mexican mush, and you could end up in the slammer.

The original faggot-tosser on Jenna's pyre is easy to identify: Elizabeth Dole. As transport secretary in the early 1980s, Mrs Dole hit on the idea of linking federal highway grants to raising the legal drinking age to 21. Sadly, even states that are supposed to take freedom particularly seriously, such as New Hampshire (motto: "Live free or die") decided to take the cash. But Jenna is not just the victim of the bossiness of a transport secretary (and failed presidential candidate). She is also swimming against two currents in American life: petty puritanism and a pathological obsession with safety.

America rightly thinks of itself as a country conceived in liberty. But it is also a country that was conceived by puritans. Again and again, these days, puritanism seems to be trumping freedom. No country treats smokers (or indeed tobacco companies) with such petty vindictiveness as the United States. As for safety, America seems to have convinced itself that the world is an astonishingly dangerous place, and that the only way to keep these dangers at bay is to regulate even the most trivial bits of behaviour. Hence the need to replace standard playground equipment with "safer" alternatives, such as one-person see-saws and transparent tubes to crawl through. And where else would photocopier toner come in packets that warn you not to eat the contents?

Of course, defenders of the current drinking laws argue that they have saved thousands of lives. But if raising the drinking age to 21 makes the roads so much safer, why not raise the age to 31? Or 51? Or ban alcohol altogether? After all, it worked so well in the 1920s. Certainly, drunk-drivers should be penalised severely. But there is no sillier use of the police's time than trying to criminalise a substance that has lubricated student life since universities were invented. And there is no simpler way of advancing liberty in America than to bring its drinking (and smoking) laws into line with common sense.

Let Jenna Bush party on. And let America rise up in revolt against all the petty princelings of puritanism, before every aspect of social life is criminalised, pathologised, regulated or legislated out of existence.

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Letters

Jun 7th 2001
From The Economist print edition

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Fact or fission

SIR – There are several imaginable scenarios for the change in energy position in the next 20 years ("A new dawn for nuclear power?", May 19th). If we are lucky, we will compensate progressively for the exhaustion of oil and gas through the construction of new nuclear reactors, transfer of fuel use and more recycling of hydrocarbon materials.

If we are unlucky and there are severe shocks to oil and gas supply from oil embargoes, Arab-Israeli wars or Gulf conflicts, secure nuclear-energy supplies could mean the difference between a local recession and the collapse of European industries and public services. It is a form of insurance and, as with all such arrangements, it is much cheaper to take out the policy well in advance of the risk being realised.

P.H. Spare
Davenham, Cheshire

SIR – While, as you note, natural gas is not an OPEC monopoly, the rapid increase in its usage for electricity production would be mirrored by increasing oil demand if France, Japan and other resource-deprived countries abandoned nuclear energy. America would suffer just the same, as OPEC oil is finite and by now we have learned what OPEC's policy is all about. American self-sufficiency is not the only issue.

Jan Bloemraad
Toronto

SIR – Your special on nuclear power is one of the more negatively biased I have seen. For example, in your chart on changing global energy use you do not mention that the heavily subsidised wind- and solar-power industries account for less than of one percent of the world's electricity consumption; nuclear power accounts for over 20%.

John Stevenson
Cleveland, Ohio

SIR – You reassure us that nuclear plants "are beginning to be run as proper businesses by serious managers." British American Tobacco is considered by some to be run as a proper business, and few of us would accuse their managers of frivolity. Yet, in the same issue ("Outrageous fortune"), you say it is in "one of the world's least socially responsible industries."

No business can be said to be good, proper and socially responsible unless it meets the following criteria. One, it is run profitably, efficiently and ethically. Two, it delivers products or services that meet real needs without damaging human health, well-being or the environment. Three, it receives no government largesse in any form, however covert, and especially not from any government that claims to be implementing large tax cuts.

David Alexander
Zeist, The Netherlands

Academic interests

SIR – As a culture of greater transparency spreads through academia, why stop with the scientists ("Outrageous fortune", May 19th)? Other academics, whether professors at business school or foreign-policy analysts, can also be swayed—or give that impression—thanks to external consultancies. While contacts between academics and the wider world should be encouraged, vested interests deserve to be aired.

All academic journals would benefit from a stricter regime. Many could do with a regime in the first place. Disclosure may not be watertight but it would do much to deter the tiny minority of downright corrupt purveyors of "independent" research.

Alexander Evans
London

Jeeves and Woodward

SIR – I am at a loss to understand the purpose of your snide remark about Shaun Woodward, a presumably wealthy Labour Party candidate, who is said to employ a butler, thus making him unfit to represent a "working-class constituency" ("On the trail", May 26th). In America, some of our wealthiest people are major contributors to the Democratic Party, and one of the best (and wealthiest) representatives of ordinary working people is Senator Ted Kennedy. Perhaps, in Britain, it is a class thing.

A.J. Sheridan
Miami

Opening the skies

SIR – I take exception to your description of open-skies agreements between America and European countries as a "sham" ("Unfinished business", May 26th). While a US-EU agreement is an ultimate goal in transatlantic liberalisation, America has been unable to negotiate with the EU as the European Commission lacked a mandate from member states to negotiate traffic rights with America. In the meantime, open-skies agreements played, and continue to play, an important role in the evolution of international aviation.

You claim that airlines with antitrust immunity (like United Airlines and Lufthansa) will conspire to cut capacity and raise fares. On the contrary, as many studies by the American government and others have concluded, prices for tickets in open-skies markets with alliances are lower than in markets without alliances. The alliance between United Airlines and Lufthansa has also made possible new services between America and Germany. Moreover, alliances offer consumers many other benefits, including additional new services.

Compare this with the restrictive market for travel between Britain and America dominated by American Airlines and British Airways. Here, a world-class airline, BMI (formerly British Midland), is prevented from flying to America from Heathrow and United Airlines is unable to increase capacity on key routes such as London-Chicago. Compared with Germany fewer new routes were opened in this market and prices per mile are the highest among transatlantic markets.

Open-skies agreements are an important and significant step in opening up international aviation markets to the ultimate benefit of the flying public. They have also allowed airlines to "test the waters" by operating in markets stripped of protectionism. Once the European Commission obtains a full negotiating mandate, these airlines would have gained necessary experience to succeed under the US-EU accord.

Shelley Longmuir
Senior vice-president, United Airlines
Heathrow Airport, Middlesex

Power cut

SIR – "Power corrupts, said Lord Acton, a Liberal peer. But loss of power, said somebody else who might as well have been talking about a Liberal, tends to corrupt absolutely", says Bagehot (May 5th). That somebody else was Pierre Trudeau, a Liberal prime minister. And he was talking about a Conservative.

Francis McInerney
New York

Rainforest conservation

SIR – You offer a generally well-balanced look at the enormous task Brazil faces in promoting sustainable development in the Amazon ("Saving the rainforest", May 12th), but some clarification is needed about the 2000-03 national-development plan, Advance Brazil.

The plan does not promote additional cutting of the rainforest. Not one *real* is allocated for deforestation but there are six programmes for environmental conservation, zoning, monitoring land use and recuperation of degraded areas, intensifying their use where appropriate. Several other programmes address social development in the region.

Moreover, Advance Brazil does not cut any new highways but merely paves existing ones. As you rightly imply, it is unrealistic to argue that the Amazon should remain untouched. Sustainable development requires a cautious but proactive approach.

Jose Paulo Silveira
Secretary of planning and strategic investments, Planning Ministry
Brasilia

SIR – Your characterisation of the economic returns to sustainable timber management in the Amazon is misleading. Years of effort and hundreds of millions of dollars in investment have failed to yield truly sustainable forestry systems because conventional logging remains financially more attractive.

Further, one needs to be clear about the distinction between sustainable timber management, which includes investments in future harvests, and reduced-impact logging (RIL), which does not. Successful forest regeneration requires actions such as maintaining seed trees, thinning harvested stands and more. Without these investments RIL is unlikely to be any more sustainable than conventional logging. If, as you say, RIL is more profitable than conventional logging, the private sector should be adopting these techniques, yet we are far from seeing a proliferation of RIL in Brazil (or anywhere else).

Eduard Niesten
Shelley Ratay
Conservation International
Washington, DC

SIR – You highlight the potential for enlightened authorities reaching a balance between economic and environmental objectives for managing forests. Such a regime was developed and operated for the last six years, by Timberlands West Coast, a New Zealand state-owned enterprise. Central government, the local community and environmentalists agreed to put land and forest of significance in the control of the Department of Conservation, with a small area of 50,000 hectares made available for sustainable indigenous forest harvesting. This was similar to RIL schemes, but even less intrusive through helicopter extraction of single specimens.

Regrettably a left-wing Labour Party bought urban votes by promising to ban the operation. They won the election, the local region lost a major developing industry and the world lost perhaps the most developed example of sustainable harvesting.

Rex Loach
Nelson, New Zealand

Sudan and oil

SIR – Jim Buckee (Letters, May 19th) asserts that there is no fighting or displacement of civilians in the Sudan oil-concession area where his company, Talisman Energy, operates. This is untrue. In April, I visited Talisman's concession area in Western Upper Nile on behalf of a number of Canadian and British non-governmental organisations. I travelled to the large part of the area that lies outside government control. Neither Talisman nor Sudan's government co-operated in this investigation. I heard numerous eye-witness accounts of attacks on civilian settlements by government bombers and helicopter gunships, government troops and progovernment militias. Several of the gunships operate from oil facilities at

Heglig, built and maintained by the consortium of which Talisman is part. This was acknowledged recently in Talisman's own compliance report, a fact that seems to have slipped Mr Buckee's mind.

Mr Buckee claims that there has been a population increase in Talisman's area of operation but the expansion is not a sign of prosperity. It is the opposite: further evidence of the violent displacement of civilians from rural areas.

John Ryle
London

Taxes and the French

SIR – It is true that most French people are pleased with their public sector ("They love it", May 26th). One reason is ignorance. When I arrived in France in 1996 from Sweden the cost of a long-distance phone call was three-times higher. Roughly speaking, it still is. Electricity too, for domestic use, costs about three times as much. Sweden gets about 50% of its electricity from nuclear plants, the rest from hydroelectric ones. France is not hugely different. The French are happy with EDF because they are unaware of how much they pay relative to consumers elsewhere.

Erik Lidstrom
Paris

SIR – It is true that a lot of public money is channelled towards France's TGV, but look what the taxpayer gets in return. A high-speed rail network covering the country with affordable ticket prices, permitting the average taxpayer to use the system without breaking his own bank balance. The British taxpayer pays far more for his ticket and gets a vastly slower service. Yet after privatisation he is still required to stump up to subsidise the network.

Nicholas Moore
St Ouen, France

Political asylum

SIR – Conservative proposals to reform the British asylum system are far from nonsensical and certainly not dishonest ("Lunatic", May 26th). The great majority of people claiming asylum in Britain are not refugees in terms of the 1951 UN convention. Last year, 10,000 applicants were found to be refugees and about 11,000 did not satisfy the terms of the convention but were, nonetheless, allowed to stay. In the same period 77,000 were rejected.

Our proposals for secure reception centres will deter unfounded claims and allow cases to be processed quickly. Those with a genuine claim will be helped to settle in Britain; those whose cases are rejected will be removed from the country. Your estimate of 25,000 reception-centre places is based on the inaccurate assumption that the average time to process new applications would be six months. Even Labour's target time for processing new asylum cases is eight weeks and the average stay in Oakington, the government's existing reception centre, is seven to ten days.

Legal and language support, asylum casework and appeal hearings would be provided on site. That, together with other procedural changes that we propose, would speed up significantly the time taken to deal with applications. That in turn will reduce the number of places needed.

Reception centres are not prisons, as you suggest. They will be similar to reception facilities used in a number of European countries. The centres will be secure at the perimeter only. Our plans are a serious proposal to reform our creaking asylum system, something which all other parties seem to be avoiding.

David Lidington
Conservative Party spokesman on home affairs
London

In the prairie doghouse

SIR – The animal pictured in your article on water in Texas ("Pay up or dry up", May 26th) is not a groundhog but a prairie dog. A prairie dog is smaller than its counterpart and is highly gregarious. Hence

two friends sneaking a drink from a pump.

K. Sitarz
Paris

SIR – We call 'em gophers down here.

Jo Schroeder
Houston, Texas

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Wanted: new rules of the road

Jun 7th 2001 | BRUSSELS AND WASHINGTON, DC
From The Economist print edition

As George Bush prepares to come to Europe, structural changes in world politics are complicating relations between the United States and its oldest friends

ALMOST ever since George Bush squeaked into the presidency last November, Europe has felt uneasy about him. In his first foreign visits and in the procession of foreign leaders through Washington, he seemed to be favouring Asia and Latin America over Europe. Then came serious disagreements: over the Kyoto accords on climate control, which America rejected to the fury and dismay of Europeans; over missile defence; over North Korea, Iraq, industrial espionage, the death penalty. America's oldest and firmest alliance now looks in trouble.

Kyoto has caused most shouting, but there are two bigger areas of difficulty. The first is defence. European governments have been rattled by America's willingness to consider deploying a national missile shield that will probably violate the Anti-Ballistic Missile (ABM) treaty between Russia and America. They do not yet know much about this shield, since the Americans have not produced a blueprint; but most do not like the sound of it. They will remain suspicious until they know whether Russia will acquiesce in the proposal and whether the shield is truly intended—as America insists—to defend only against threats from regimes such as North Korea's. If it is, their worries might recede.

Divisions over missiles are exacerbated by lurking disagreements over conventional forces. Some Pentagon planners want to redeploy to the Pacific up to a third of the 120,000 American troops now in Europe. If Mr Bush approves, Europeans might think America was abandoning them. For their part, Americans are sceptical about the European Union's plans for a rapid-reaction force. Could such a force be smoothly integrated into NATO? And will Europe stump up enough money for it? If not, Americans fear that the new European security and defence policy could end up operating at NATO's expense.

Divisions over missiles are exacerbated by lurking disagreements over conventional forces

After defence, trade still causes many a headache. Transatlantic trade disputes have spread from beef and bananas to regulatory matters, once the province of domestic policy, that touch on different cultural assumptions. (How much noise should planes be allowed to make? When does food production become "unnatural"? How much should privacy be protected?) The two sides are encouraged by the recent settlement of their long dispute over bananas, and the two trade negotiators, Pascal Lamy and Robert Zoellick, get on well. But that is no guarantee of peace.

American steel producers, for example, are seeking more protection, and on June 5th Mr Bush took the first steps towards imposing new measures to deter steel imports. In 2003, too, an EU-American moratorium on new complaints about farm trade is due to expire (see article). Americans are incensed about European-led efforts to shut down "unfair" tax havens. Some Europeans accuse America of using the surveillance capabilities of its national security agency to conduct industrial espionage. And if the World Trade Organisation rules against the United States in a case the EU has brought against its foreign-sales corporation tax, the EU could impose $4 billion-worth of sanctions—a threat Mr Zoellick

describes as “nuclear”.

The worry is that behind individual disputes may lurk a broader failure, to agree on a new trade round. Both America and the EU say they want one, but they disagree over whether competition policy and investment should be included. Their underlying differences, rather than stone-throwing anarchists or the objections of India and Brazil, were the main reason for the failure to launch a new trade round in December 1999.

Dangerous stereotypes

When things are going well, Europeans and Americans slap each other on the back, talk about common values and boast that they are the world’s joint bulwark in the championing of human rights, trade and democracy. When things go badly, they fall back on some surprisingly negative stereotypes.

The American stereotype is of a Europe that is economically sclerotic, psychologically neurotic and addicted to spirit-sapping welfare schemes and a freedom-infringing state. The European stereotype is of a gun-slinging, Bible-bashing, Frankenstein-food-guzzling, behemoth-driving, planet-polluting United States, in which politicians are mere playthings of mighty corporations.

These stereotypes exist not only in the public imagination, but in the halls of power. “European” is such a bad word to some in the Bush camp that a Bush strategist once got a reporter in Texas reassigned for referring to one of her boss’s economic schemes as “European-style”. Across the Atlantic, one EU commissioner says he is “quite convinced that Bush’s policies on missile defence and Kyoto were dictated by campaign donations from big corporations.” Here lies perhaps the most striking recent change in the transatlantic relationship. European assessments of America, which tend to mix admiration and criticism in equal parts, have been usurped by assessments of Mr Bush himself, which are strongly hostile.

A reporter was once reassigned for referring to one of her boss’s economic schemes as “European-style”

The shadow cast by Mr Bush, however, is a reminder of the need for caution when judging transatlantic relations. In his diaries, Helmut Schmidt, the then (West) German chancellor, said that the debate over American demands for the installation of nuclear weapons in Europe during the 1970s and 1980s came close to threatening democracy on the continent. Today’s disputes may be about the future of the relationship, but they do not threaten its existence.

Moreover, there are signs of a repeating pattern. Many of the things now being said about Mr Bush were said in the early days of the Clinton administration. Europeans then complained of the Helms-Burton Act, which applied American sanctions extraterritorially against foreign companies. They disliked America’s refusal to pay its United Nations dues, its reluctance to ratify a convention on anti- personnel mines and its refusal to join the International Criminal Court (all matters on which Mr Clinton broadly took Europe’s view, but could not persuade Congress). Later, they criticised the Senate’s rejection of the Comprehensive Test Ban Treaty and Mr Clinton’s interest in missile defence. Yet by 2000 Chris Patten, the EU’s commissioner for external affairs, could say: “Europe will miss Bill Clinton. He has been a good friend to this continent.”

Perhaps European opinion will alter to accommodate Mr Bush in the same way. But don’t count on it. Mr Bush may have toned down his determination to pull out of the ABM treaty, but he is likely to remain more enthusiastic about points of European neuralgia than Mr Clinton ever was. More important, structural changes in world politics are driving a wedge between Europe and America more deeply than in the early 1990s.

Shifting world, strained alliance

The most visible difference is that, among Europe’s four big powers, only the incoming government of Silvio Berlusconi in Italy now officially shares Mr Bush’s conservatism. In contrast, Germany, France, Britain, Italy and most EU countries had nominally centre-left governments during much of Mr Clinton’s presidency. Tony Blair adored his third-way seminars with Mr Clinton and an assortment of European social democrats. There will be no such transatlantic love-ins with the Republicans in the White House.

Such changes may be merely cyclical. Others may last longer. In 1993, Western Europe was struggling with its worries about a united Germany. The Balkans had just exploded and European policy there had failed. The big worry was of an isolationist America. Now the Balkans, though hardly stable, are at least not at war, and the implications of the Soviet collapse are clearer. America, uniquely powerful, has less need of European support, at least in the old way, while Europe, freed to concentrate on its grand project of ever-closer union, no longer need defer to America as it once did. The EU is closing in on its ambitious goal of incorporating most of the countries of East and Central Europe; its single currency, the euro, will be issued in notes and coins in January; and its efforts to forge a common foreign and defence policy are being beefed up.

Europe, freed to concentrate on its grand project of ever-closer union, no longer need defer to America as it once did

In all these areas, competition with the United States is a tacit reference point. When the euro was set up, it was seen as a potential reserve currency to challenge the dollar; its downward slide against the greenback is followed neurotically. Eastward enlargement is praised because it will create a single market of 500m people, almost double "you-know-who". The success of the joint foreign policy is gauged by how far the EU can match American influence in the Middle East or the Balkans.

The result has not been too bad for the main institution of the transatlantic alliance. Some had expected NATO to wither away with the end of the cold war. Instead, by absorbing members of the former Warsaw Pact, it has transformed itself from an alliance to defend West European territory into the would-be guarantor of security throughout the continent. The Kosovo operation, a huge multilateral military campaign, was the first successful item on this new agenda.

But the more important upshot of the consolidation of Europe has been to tug Europe and America in opposite directions. Ivo Daalder of the Brookings Institution, a Washington think-tank, argues that the two sides look at the world in increasingly different ways. Most obviously, they are interested in different parts of it. As the debate in America makes clear, the need for global missile defence is driven largely by Asia: most immediately by North Korea's long-range missiles, further off by China's nuclear arsenal. Mr Bush himself has claimed that his other top policy priority is the consolidation of democracy and free markets in the Americas.

The upshot of the consolidation of Europe has been to tug Europe and America in opposite directions

In contrast, Europeans are focused more and more on Europe itself. The Atlanticist generation of Margaret Thatcher has largely passed, and the continent is dominated by political leaders whose lives have been shaped by the debate over the EU. There are exceptions to this rule—notably Javier Solana, the EU's high representative for foreign policy, a former head of NATO and a firm Atlanticist—but for the most part it is the shape of the EU, as discussed recently in competing speeches by the French and German leaders, that seems likely to absorb Europe's interest for the foreseeable future.

Differences in geographical focus are only part of the emerging division between Europe and America. More profoundly, the two sides approach the world with different mindsets. The European project is a product of international treaties, of collective institutions and mutual entanglements. By binding themselves to one another even in the face of short-term difficulties, Europeans believe that they have made themselves better off economically and think that they will one day do the same in security terms. (Britain, as usual, is a partial exception to this view.)

So when Europeans search for a common foreign policy, they naturally apply the principles of multilateralism that have worked well at home. Hence their interest in the "new agenda" of borderless problems such as global warming, international crime and disease. Hence their almost hysterical reaction to Mr Bush's rejection of Kyoto.

In contrast, Americans in general—and the Bush administration in particular—tend to see the world in traditional great- power terms. National interest, diplomatic leadership and the projection of military might are what matter. International treaties and global norms merely constrain America's sovereignty. When Mr Bush junked the Kyoto treaty, he did not argue that the treaty was a bad way to tackle global warming; he said that its costs were greater than America wanted to bear.

Seen from European capitals, the problem is one of American unilateralism. Put crudely, many Europeans think that the United States feels that it is big enough and strong enough to ignore international rules when it finds them annoying. Even Britain, which in moments of crisis usually sides instinctively with the

Henry Kissinger has worried that some Europeans

United States, shares this view. Americans, on the other hand, often see Europeans as grandstanding free-riders, willing to lecture America about the death penalty but less willing than they should be to spend the money to make their troops effective. Henry Kissinger, for one, has worried that some Europeans are trying to use antagonism towards the United States as a way of defining their own identity.

are trying to use antagonism towards the US as a way of defining their own identity

As a result, the old basis for the transatlantic relationship has gone. Once, as Mr Daalder puts it, "Washington could presume that if it led, Europe would invariably follow." Now, the consultation and trust that underpinned the relationship cannot be taken for granted. As one example, America announced recently that it would sell diesel-powered submarines to Taiwan. America does not make these submarines; Germany and the Netherlands do. But America did not consult them before it made the generous offer. They declined to fill the order.

Diverging, converging

At this point, the transatlantic relationship is at a point of divergence. What are the consequences of the different paths it might take?

The relationship will not break down in acrimony. Despite all the problems, the institutional, economic and cultural ties between America and Europe remain stronger than those between America and any other parts of the world. These ties set a limit to further deterioration. On questions of war and peace, America and Europe will presumably continue to act as one. But in the absence of an all-consuming Soviet threat, such questions are unlikely to present themselves. And on the immediate geopolitical issues, such as how to draw China and Russia into the family of democratic nations, America and Europe do not see eye-to-eye.

The more likely outcome, therefore, is continuing drift. This would not be a disaster, but it could have substantial opportunity costs. American policy towards China and Russia would be hampered. So would dealing with a revived Iraq, or sudden crises in the Middle East or Africa. Continued drift will make it harder to settle the disputes over defence, trade and global warming. And it risks developing, after a decade or so, into a slow unravelling that might be as dangerous as an open split.

There remains a third possibility, a revival of the transatlantic alliance. In the post-cold-war era, that would mean creating a partnership of equals out of an American-dominated defensive alliance. Such a partnership will not be easy to achieve, given the political differences and the lack of deference. But it should be possible. An American gesture of conciliation over Kyoto would be a useful start.

In principle, Europe's new military ambitions could dovetail with America's desire to concentrate more on Asian security. If the Americans make it clear they have no intention of abandoning Europe, and the Europeans stress that they are not setting themselves up as strategic rivals, the two could work in harmony. The EU's economic muscle should also make it easier to deal with future financial meltdowns such as the Asian crisis of 1998. The question is whether such burden-sharing would strengthen the alliance or merely paper over the cracks.

In principle, Europe's new military ambitions could dovetail with America's desire to concentrate more on Asian security

Europeans are already showing that, despite their introversion, they are prepared to act in ways that help the United States outside Europe. An early test came in North Korea. There, Mr Bush interrupted international efforts to get the hermit kingdom to abandon its missile-selling ambitions by demanding greater openness. A subsequent EU mission helped keep diplomacy on track. If—a big if—American toughness and European helpfulness can be combined, the two might get the best of both worlds. For the immediate future, there are hopes that Mr Bush's trip to Europe may produce a joint approach to the Middle East, laying to rest notions that the two sides are in competition there.

Europeans often justify the need for multilateral institutions by citing the contrast between the aftermath of the first and second world wars. Since 1945, a host of multilateral bodies—the UN, NATO, the GATT, the IMF and World Bank, the EU itself—have fostered world trade and security. In contrast, the fledgling multilateral institutions set up after 1918 collapsed, partly because of American isolationism and protectionism. The implied concern is that American unilateralism today will do what American isolationism did after 1918, and undermine efforts to forge a more stable and prosperous world.

Yet no sooner is the fear stated, than it can be seen to be overplayed. America is not the best of friends with the UN; but it is hardly threatening to withdraw from it. It is committed to EU enlargement, is keener on NATO expansion than many Europeans, and has learned to live with the WTO. At a time when American-European arguments are proliferating, and when both sides often seem more preoccupied by other relationships, it is as well to remember how much they still have in common, and what they could do together if they put their minds to it.

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The mayoral election in Los Angeles

Is he up to it?

Jun 7th 2001 | LOS ANGELES
From The Economist print edition

EPA

James Hahn's victory this week shows the limits of Latino power; but the new mayor will be judged by whether he can make the city work

Get article background

THE Latino ascendancy seems to have been postponed—again. The next mayor of Los Angeles, where Latinos make up 46% of the population, will be James Hahn. The city attorney beat his fellow Democrat, Antonio Villaraigosa, who was seeking to be the first Latino mayor of the city since 1872 (when the place was a village in the desert), in a run-off election on June 5th by 53.5% to 46.5%. In April, Mr Villaraigosa, the speaker of the state Assembly, had finished ahead of Mr Hahn in the first round of voting; he also went into the election with the support of both Richard Riordan, the outgoing Republican mayor, and Gray Davis, the governor of California. But he did not prevail.

The mechanics of Mr Hahn's victory were somewhat feudal. He built his campaign on a foundation of loyal support among black voters, who treasure the memory of his father, Kenneth Hahn, staunch for their interests during his 40 years as a county supervisor. He also did well with another traditional power block—white conservatives in the San Fernando Valley, the northern part of the city. Meanwhile, he split the liberal vote with Mr Villaraigosa. His rival won among Latinos, who accounted for 23.6% of the total turnout, and trade unionists.

The blast of political buckshot that supposedly slowed down the Villaraigosa bandwagon was a Hahn TV ad shown two weeks ago. It drew attention to a letter Mr Villaraigosa had written to Bill Clinton requesting a pardon for a cocaine dealer whose father had contributed to his campaign, but it did so by juxtaposing pictures of a crack pipe with Mr Villaraigosa's face. Critics say that Mr Hahn was summoning up racist stereotypes of Latinos from the gang-ridden neighbourhoods of East Los Angeles, where Mr Villaraigosa grew up.

Anger at Mr Hahn's attack may have driven more Latinos to vote for Mr Villaraigosa. But there is little evidence that his race was an issue with white voters. Most whites know very well that a Latino mayor is inevitable sooner or later. Another Latino, Rocky Delgadillo, was elected to citywide office as city attorney. He, however, was strongly pro-business and had fewer ethical shadows.

Whites rejected Mr Villaraigosa largely because, despite Mr Riordan's endorsement, he appeared to be more left-wing than Mr Hahn: softer on crime, more friendly to trade unions and less likely to shake up the city's entrenched bureaucracy. That he allowed Mr Hahn, a soft-spoken apparatchik, to beat him speaks more about Mr Villaraigosa's campaign than the future for other Latino politicians.

Now to work

When he takes office on July 1st, Mr Hahn will have more power at his disposal than any of his

predecessors. That does not say a great deal. The Progressives who wrote the city charter in 1925 did so with a wary eye on the political machines that ruled big cities back east. They divided up power between the mayor and a city council, and they also gave great independence to agencies such as the police. The result was frequently political paralysis.

Two years ago, Los Angeles voters approved a modified charter that increased the mayor's powers. He can now hire department heads and appoint the commissioners who supervise departments, and he needs the votes of only eight out of 15 councillors to confirm them. He can also fire most department heads and commissioners without council approval—except in the most important departments, such as the police, where it takes ten commissioners to overturn his wish.

Mr Riordan, the outgoing mayor, chose not to flex his new muscles during the final two years of his tenure. Mr Hahn will have to deal with a city council with eight new members, all as unsure of the state of play as he is. Another centrifugal force comes from the newly created neighbourhood councils, which give voice to the concerns of still smaller subdivisions within the city. Mr Hahn will still have to negotiate, cajole or chivvy to get his way.

The Los Angeles Mr Riordan passes on is also a different city from the one he inherited. Eight years ago, the combined aerospace and defence industries were the city's largest employer. Today, aerospace and high-tech employment has fallen to 200,000, while employment in businesses related to international trade, such as banking and warehousing in the region's ports, has risen to 420,000.

Big firms have pulled out, leaving Los Angeles as a city of small and medium businesses: 95% of the firms in Los Angeles County employ fewer than 50 people. Many of these firms are part of the largest urban concentration of manufacturing in the country, making toys, furniture, clothes and high-tech parts for what remains of the aerospace industry.

This structure may have helped make LA an ever more international city (even Hollywood now makes more of its money abroad than in America). But such a diverse, diffuse collection of businesses does not create natural leaders. There are precious few commercial cheerleaders for LA. Under Bill Clinton, California could always count on a little support from the White House. Mr Bush reputedly takes the ABC tack—"Anywhere But California".

With little help forthcoming from outsiders, Mr Hahn has two big local challenges to sort out with the city council. The first is improving municipal services. The Reason Public Policy Institute recently produced a study of the efficiency with which 44 big American cities deliver such basic needs as police, fire and ambulance services. Los Angeles came bottom.

The study also revealed that civic efficiency tended to be highest where there was more political accountability for their delivery. Charter reform may help Mr Hahn a little with the Los Angeles Police Department (LAPD), which is still wrestling with a corruption scandal. He will have to enforce a new regime of federally imposed oversight, and also decide whether to reappoint the current chief, Bernard Parks. The other "service" that infuriates Angelenos—the woeful school district—is less within the mayor's control.

These inadequacies tie into Mr Hahn's second great challenge, which is to keep the city together. Malcontents in the San Fernando Valley, home to around 40% of its population, want to secede and form a new city with its own taxes and services. Separated from the rest of Los Angeles by the Hollywood Hills, they complain that the city government funnels far more out of the Valley in taxes than it ever returns in the form of transport (the city subway never got this far) and law enforcement. Critics detect a racist element to the separatist movement. But, on paper, a San Fernando Valley city would be no more illogical than existing cities such as Beverly Hills and West Hollywood.

Mr Hahn's tactics are likely to follow those of his predecessor. Mr Riordan was a master of the backroom chat. But he could talk to businessmen as an equal, in wealth and in experience; Mr Hahn cannot. The one thing he does know is city politics. Given the size of the problems that now confront the city, backroom deals may not be enough any more.

Mr Villaraigosa's supporters will argue that their more charismatic candidate would have been a better problem-solver than Mr Hahn. But on many of the thorniest issues, such as whether to reappoint Mr Parks at the LAPD, the two men competed only to out-waffle each other. Mr Hahn has at least the advantage of knowing Los Angeles' weaknesses better than anybody else. With luck, he could be the city's Mikhail Gorbachev and tear down the system that created him. But don't bet on it.

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Tobacco and the courts

Butt surely not $3 billion?

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A California jury has punished the firm that sold a cancer sufferer his poison

ONE reason that Angelenos like the privacy of their cars is that they can smoke in them without the sanctimonious disapproval of their neighbours. The tellings off which smokers must endure in California are as nothing, however, compared with the punishment just dished out in Los Angeles to Philip Morris. On June 6th a jury in the LA County Superior Court ordered America's largest tobacco firm to pay $5.5m in compensation to Richard Boeken, a smoker with cancer—oh, and a cool $3 billion in punitive damages.

The fine is by far the largest ever imposed on the tobacco industry in a lawsuit brought by an individual, dwarfing even the $79.5m in punitive damages imposed in a case in Portland, Oregon, in 1999. Those damages were later reduced by the judge, and Philip Morris's furious lawyers are hoping for the same thing in Los Angeles.

Ironically, the firm had taken a softer approach in court than previously. Other cases have forced stacks of internal tobacco-company documents into the public realm, making it harder to sustain the bland claims of ignorance with which the industry fought off lawsuits so successfully in the past.

Acknowledging past wrongdoing gained Philip Morris no mercy, however. The jury found it guilty on all six of the charges brought by Mr Boeken, including fraud, conspiracy and negligence. He claims to have picked up his habit 43 years ago, as a 13 year old (before health warnings appeared on cigarette packets, though not before smoking was widely known to be bad for you), and to have been unable to shake it, despite kicking addictions to both heroin and booze.

From the industry's viewpoint, the case confirms California's role as tobacco's Torquemada. Big Tobacco has now lost three cases in California. Whatever the industry claws back on appeal, the Boeken case has prised the breach in its defences a little wider. On the other hand, the Golden State's holier-than-thou approach to health has helped bring smoking—and lung cancer—to the lowest level in the country.

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Trade policy

Steely resolve

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What's politically useful at home may be dangerous abroad

IN POLITICS, as in comedy, timing is everything. President George Bush announced on June 5th that America would begin investigating unfair trade practices in the global steel industry, with the intent of imposing new anti-dumping duties on imports. Mr Bush had an important domestic reason for acting when he did, but he also risks alienating his trading partners at a crucial time.

The newly empowered Democrats in the Senate were about to steal Mr Bush's thunder. America's steel makers have long been lobbying for an anti-dumping investigation, and Max Baucus, a Democrat from Montana, was planning to ask for it as he took over the Senate Finance Committee. Mr Bush hopes to use the investigation, which is likely to result in protective duties, as a sop to organised labour to help his push in Congress for trade-promotion authority, the speeded-up negotiating powers once known as fast-track.

For this reason, Mr Bush's cabinet has been looking into the possibility of an investigation for months. The treasury secretary, Paul O'Neill, commissioned a private study of the steel trade from the Boston Consulting Group early in Mr Bush's term. In April America's trade representative, Robert Zoellick (normally a devout free-trader), lent support to the idea of protecting the steel industry as long as it continues "moving in the right direction", which is apparently towards attrition. Donald Evans, the commerce secretary, asserted in May that America would ensure a "level playing field" for its steel companies.

The investigation, under the notorious Section 201 of the Trade Act of 1974, immediately came close to torpedoing the administration's new two-way policy on China—warm on trade, cool on security. American and Chinese trade negotiators were locked up this week in Shanghai, trying to resolve the level of agricultural subsidies China would maintain after joining the World Trade Organisation (WTO). China's top WTO negotiator, Long Yongtu, said he would wait and see whether the American action complied with the global body's rules before reacting. But Chinese steel companies, which account for 7% of America's imports and are already the subject of anti-dumping complaints there, condemned Mr Bush's move.

The reaction from Europe was also hostile. Shares in steel makers fell as talk circulated of the European Union challenging any American curbs on imports at the WTO. Pascal Lamy, the European Union's trade commissioner, opposed Mr Bush's action; he had been hoping for multilateral talks on steel.

The other parts of the president's plan for the steel industry are agreeably multilateral: he wants Mr Zoellick to negotiate a cut in excess capacity and eliminate government subsidies in the steel industry worldwide. David Phelps, president of the American Institute for International Steel, sees those as positive developments. But he would have preferred Mr Bush to encourage America's steel firms to take part in the merger wave that has lately swept the globe, rather than squawk for more protection.

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Lexington

Theodore McCain

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From The Economist print edition

Will the Arizona maverick imitate his hero?

DURING last year's presidential campaign, Karl Rove, George Bush's chief political adviser, went around touting the notion that the 2000 election would be a rerun of the vote of 1896. Just as William McKinley, he claimed, had ushered in an era of Republican dominance by appealing to both the power of corporate interests and the votes of the new industrial working class, so Mr Bush was supposed to combine traditional Republican business interests with the votes of new-economy workers to form a big governing majority. It didn't happen, of course. But resemblances to the politics of 100 years ago have made a surprising comeback, this time with to the events of 1912.

In that year, Theodore Roosevelt, who had earlier been McKinley's vice-president and then president himself until 1909, lost the Republican nomination to the incumbent, William Howard Taft, despite winning the popular vote in the primaries. (Those were the days when the real choice was made in smoke-filled rooms.) Roosevelt stormed out of the Republican Party, and six weeks later returned to fight the election under the banner of the newly formed National Progressives, better known as the Bull Moose party. His campaign remains the high point of third-party politics in America. Roosevelt beat Taft into third place but, by splitting the Republican vote, let in Woodrow Wilson, the Democrat, as president.

Now cut to a self-proclaimed Roosevelt fan, John McCain. Mr McCain also scored a popular hit in the 2000 presidential primaries, though he didn't win them. Unlike Roosevelt, he has stayed in the Republican Party. But in the aftermath of Jim Jeffords's defection and Mr McCain's "coincidental" decision to invite Tom Daschle, the Democratic leader in the Senate, to stay for the weekend in Arizona, it is hardly surprising that rumour has Mr McCain thinking about doing a Roosevelt and hoisting the banner of independent reform for the 2004 election.

He is thinking about it, almost certainly. He knows his chances of being the Republican presidential candidate in 2004 are zero. Even when the presidential nomination was open, he could not persuade party loyalists to stray from Mr Bush. He stands no chance next time, except in the extraordinary event that Mr Bush chooses not to run again. Nor could he plausibly run as a Democrat. Though he is less reliably right-wing than he was, Mr McCain is a conservative. On the scale of one to 100 drawn up by the American Conservative Union to measure Senate voting records, Mr Jeffords scores 36; Mr McCain, 81.

But he might—just—stand a chance as an independent. Say Mr Bush's presidency was widely seen as having failed by 2004, because the economy was in the tank. Say also that the Democrats react by turning left—perhaps by nominating Al Gore to run again on a soak-the-rich ticket. In such circumstances, the usual reservations that doom third-party candidacies to failure might not seem so compellingly ominous.

For the moment, Mr McCain says he will not leave the Republican Party. Indeed, he has no need to do so. Becoming an independent now would not boost his influence over the Senate, but would reduce further any sway he has in the White House. All he needs to do is manoeuvre himself into a position from which he could make a break if he wanted. That gives him plenty of time to study Roosevelt's experience.

Roosevelt was one of the most charismatic presidents in history. A war hero, he led a cavalry charge up Kettle Hill in the battle of San Juan. A larger-than-life figure and a great preacher from the bully pulpit, he was shot in the chest during an election rally in 1912. The bullet was deflected by his notebook and Roosevelt, roaring that he was as strong as a bull moose, recovered to make a speech. Mr McCain's

appeal hardly reaches such heights. But his personal history and his televisual forthrightness are cut from similar cloth.

More important, the two men share a common ideology. Notions of national greatness are important to Mr McCain too. Both support deep American engagement abroad and vigorously defend the virtues of national service and the projection of military force (“Speak softly and carry a big stick”, said Roosevelt.) Domestically, Mr McCain is trying to revive the Roosevelt tradition of “progressive Republicanism”. The starting-point for both is that the Republican Party has become the captive of special interests. Roosevelt passed the first campaign-finance reform and instituted the first big antitrust cases. Mr McCain, in a more modest way, has used his chairmanship of the Senate Commerce Committee to push for an end to corporate welfare.

The big difference is that Roosevelt pursued his policies as president, a position he reached from within the ranks of the Republican Party. When Roosevelt tried to continue his crusade as leader of a third party, he failed comprehensively. After losing the election, he rejoined the Republicans in 1916—and the remnant of the Progressive movement was mopped up into the Democratic Party by Theodore’s cousin, FDR.

Mr McCain could try to claim to himself that modern politics is making a third-party bid ever easier. Party identification is falling among voters, and more than a third of Americans describe themselves as independents. Ross Perot won a fifth of the vote in 1992. But the harsh fact is that Roosevelt had more backing. In the early 1900s, there were half a dozen Progressive or independent senators from the mid-west and California, both of which had strong third-party movements. There are none now, except Mr Jeffords and two governors, Jesse Ventura of Minnesota and Angus King of Maine. Republican senators who supported Mr McCain in his 2000 bid would probably desert him if he were an independent. Unlike his hero, Mr McCain would be starting almost from scratch.

All these would be good reasons for the Arizona maverick not to take the same route as his hero. But, being just as indifferent to danger, he may not pay any attention to that.

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The Florida recount

Unfair, again

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A stinging report on the shenanigans in Florida is too partisan to be credible

THE Florida recount is like one of those monsters in a horror film that, just when you think it is dead, pops up again in yet another mutation. This time the monster is in the form of a searing report from the Commission on Civil Rights.

It says that Florida's conduct of the 2000 election was characterised by "injustice, ineptitude and inefficiency". A combination of unequal access of up-to-date voting equipment and "overzealous efforts" to purge voter lists of ineligible voters such as felons hit blacks harder than any other group. Blacks were ten times as likely as whites to have their ballots rejected. A full 54% of the votes rejected during the Florida election were cast by them.

The report criticises both Jeb Bush, the governor who also happens to be the president's brother, and Katherine Harris, the secretary of state. The commission is poised to ask the Department of Justice and the Florida attorney-general's office to investigate whether federal or state civil-rights laws were violated.

Much of this is old hat. Everybody knows that much of America's voting machinery is a disgrace. And everybody knows that the worst voting machinery is concentrated in poor areas. But the Civil Rights Commission report still matters for two reasons. First, the commission has spent longer studying the subject than anybody else. Second, it has focused exclusively on the most explosive charge in the whole Florida fiasco: that minorities were systematically punished.

But the commission has left itself open to the charge of partisanship. It consists of four Democrats, three independents and one Republican. And two of the nominal independents were appointed by Democrats, including the commission's chair, Mary Frances Berry, who has contributed to both Hillary Clinton's and Al Gore's political campaigns. Abigail Thernstrom, the commission's lone registered Republican, has no hesitation in dismissing the report as "totally partisan".

The commission also failed to give either Governor Bush and Ms Harris, or indeed its own members, the customary 30 days to consider their replies. Mr Bush had to reply to a flurry of (leaked) newspaper headlines before he received the full report. Ms Thernstrom was only given three days to read the report.

The substance is also questionable on three counts. First, the commission concentrates on race at the expense of education levels and voting experience. Spoiled ballots were concentrated in areas with high levels of illiteracy and with large numbers of first-time voters. Levels of illiteracy are roughly twice as high among blacks than whites, and 40% of the blacks in Florida were first-time voters. (And despite all the loose talk about structural racism, it is worth remembering that blacks made up 16% of voters, though they account for 11% of the registered voters.)

Second, laying so much blame on the governor and secretary of state is unrealistic. The voting system in the United States is highly decentralised. Most of the key decisions were made in Florida's 67 counties rather than in Tallahassee. Many of the counties with the highest number of voter errors were under Democratic control.

Third, the commission is far from even-handed when it comes to dealing with felons. It focuses on the 1,000 or so ex-offenders who were erroneously kept off the voting roles. But two Florida newspapers have demonstrated that more than 5,000 felons who are not legally entitled to vote managed to do so anyway.

Democrats will seize on the report to question the legitimacy of George Bush's presidency. It will also fan fears among blacks. But even the commission admits that there is no "conclusive evidence" that officials "conspired" to disenfranchise minority voters. That could have done with slightly more prominence.

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Gastronomy

In cod we trust

Jun 7th 2001 | NEW YORK
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A British import wins surprising favour

IN NEW YORK, a city where respectable people are driven to bribing waiters in the vain hope of getting a table at restaurants like Nobu, stodgy British grub should have no place. Yet fish and chips, that highlight (some say) of British cuisine, is the latest fashion from across the Atlantic to sweep into New York.

English Harbour Fish & Chips has recently opened two outlets in Manhattan, and Park Slope, a trendy Brooklyn neighbourhood, has become the home of The Chip Shop. Now comes, ho ho, A Salt & Battery, a new chippie in Greenwich Village run by the folks who brought you Tea & Sympathy, an English restaurant that for the past decade has been serving up boarding-school staples such as shepherd's pie and treacle pudding. Although not everybody's cup of tea (on a bad day, the service can be as churlish as any greasy-spoon in Barnsley, circa 1972), its products and style are said to be enjoyed by Anglophile masochists such as Quentin Tarantino.

A Salt & Battery caters to a similarly eclectic crowd, says Nicky Perry, who owns both restaurants with her husband, Sean Kavanagh-Dowsett. The expatriate crowd is leavened by plenty of locals, who come to sample items like chips with curry sauce, and fried Mars bars, a delicacy unknown outside Scotland and out of fashion even there. "We get lots of Irish policemen. And every construction worker in downtown Manhattan is here at lunchtime."

Some care is taken with verisimilitude. The staff are cheery cockneys (that's where they've all gone), the feast comes wrapped in faded copies of the *Independent*, and the chips, cut with a genuine British potato chipper, are of different sizes. This can distress Americans, used to standard-length McDonald's fries; one diner sent his back, worried that they did not match.

On the other hand, New York pretension is not forgotten. Black-and-white photographs of depressed pensioners in deckchairs hang on the walls (there's little chance of meeting the real thing). The restaurant has an alcohol licence allowing it to serve Boddington's and Newcastle Brown ale (in Britain, a flat Coke would normally wash things down). The last upmarket touch is the bill: $10.49, about £7.30, for a portion of cod and chips.

Ms Perry is now looking for investors, to help turn the brand into a chain. How successful they will be remains to be seen. New Yorkers are a fickle lot, especially when it comes to food. Restaurants—rather like chips wrapped in newspaper—rarely remain hot for long.

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Pension reform

Straight talk on Social Security

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The gloomy prospects for reform are exceeded only by its importance

ON JUNE 11th, President George Bush's Social Security commission will hold its first meeting. Chaired by Patrick Moynihan, a former senator from New York, and Dick Parsons, co-chief operating officer of AOL Time Warner, this 16-member bipartisan group continues a venerable tradition of panels created to advise on America's most contentious public-policy issue—pension reform. With the exception of a commission chaired by Alan Greenspan in 1983 that resulted in a hike in both the payroll tax and the retirement age, most have had precious little impact. Unfortunately, this group may fare no better.

One reason is the political calendar. The commission has to have recommendations ready by the autumn. But that is still only one year away from the 2002 mid-term elections. Republican lawmakers are hardly likely to want to debate such a hot topic in the run-up to the polls. And with the Senate now in Democratic hands, it is unlikely that they would be able to anyway.

Nor does the nature of the commission itself bode well. It is composed largely of technical experts rather than political constituencies. To be sure, there are former legislative heavyweights, notably Mr Moynihan. But, unlike Mr Greenspan's commission, it contains no sitting members of Congress and nobody who obviously speaks for the elderly.

Moreover, say detractors, the very remit of the commission suggests its purpose is political rather than practical. Mr Bush has instructed it to look at the kind of reform proposals he favours—especially the creation of individually controlled, voluntary personal retirement accounts. Both the Democrats and Republicans on the panel support individual accounts, even though they are still controversial. Without the full spectrum of views, it is argued, this commission will have no mandate and go nowhere.

Perhaps. But it could just be that Mr Bush has hit on a cleverer formula: use a respected bipartisan group of technocrats to flesh out a workable reform proposal before it gets bogged down in political sloganeering. With luck, this commission could bring the idea of individual accounts even further into the political mainstream. But in doing so the commission will clarify economic realities that Mr Bush may not like.

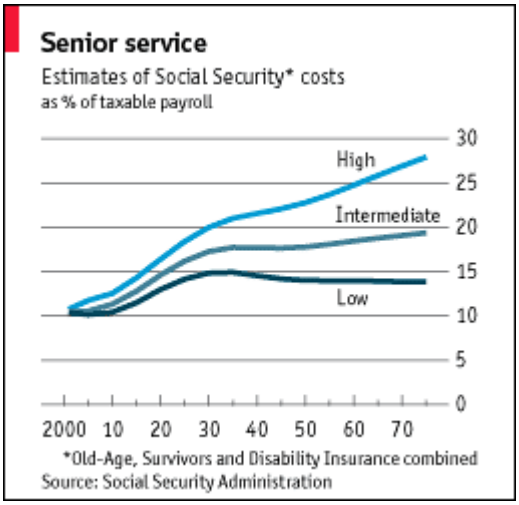
The panel's goal is to "restore fiscal soundness" to America's pension programme. It is now widely known that the ageing of the baby-boomer generation will put unsustainable pressure on America's retirement plan. In 30 years there will be twice the number of elderly with only 15% more workers. Less well known is that increases in longevity and a continued low birth rate mean that Social Security's finances look parlous well beyond the baby-boomers.

In 30 years there will be twice the number of elderly with only 15% more workers

According to Social Security's actuaries, the "intermediate", or most likely, scenario suggests that the payroll tax would need to rise from 12.4% to more than 19% in 2075 to pay future pensions (see chart). And the trend would still be upward. Moreover, the economic impact of such dramatic tax hikes (even if they were politically feasible) would make matters even worse. Truly fixing Social Security therefore goes well beyond the baby-boomer generation.

Creating a system based partly on individual accounts, as urged on the commission by Mr Bush, is one way to do this. Individual accounts help to create a "pre-funded" retirement system, where workers' retirement money is put aside in advance. America's current system, in contrast, is pay-as-you-go: today's workers pay for today's retirees (although, to complicate things, the build-up of surpluses in the Social Security trust fund has made it

partly pre-funded). Private accounts give an individual greater control over the assets. But, importantly, it is the pre-funding rather than the private nature of the accounts that makes such retirement plans more sustainable in the long term.



Nonetheless, many Democrats and elderly Americans are deeply suspicious of individual accounts. They worry that risks will increase; that the pension system will become less redistributive; that the administrative costs will be prohibitive; and that private accounts make Social Security's financial problems even worse. The commission needs to address these issues.

Today's Social Security system is a relatively ineffective form of redistribution

Some of these worries are overblown. Recent academic research, for instance, has shown that today's Social Security system is a relatively ineffective form of redistribution. While poor people do get a relatively higher proportion of their working salary in retirement cheques than richer ones, this redistribution is largely offset by the fact that rich people tend to live longer, and by the benefits their spouses receive. (Since spouses receive half a worker's retirement benefit, rich spouses get relatively more than poor ones). Recent research by two Harvard pensions experts, Martin Feldstein, a Republican, and Jeffrey Liebman, a Democrat, shows that, if carefully designed, virtually everyone, including the poor, would be better off under a mixed system that included individual accounts as well as Social Security.

In the small print

Nonetheless, there are important design details. Do you, for instance, force people to annuitise the assets in their accounts when they retire, so that they receive an annual payment rather than a lump sum? Annuitisation again favours the wealthy, because they live longer. But without it, some people might simply blow their nest eggs. By concentrating on these design details, the Bush commission could defuse some of the unnecessary political hysteria around individual accounts.

The biggest problem is financing. In essence, a shift from a pay-as-you-go system to one that is even partly pre-funded means that one generation of taxpayers must pay twice: once to pay for their parents' Social Security cheques, and again to build up their own private accounts. In practice this "transition cost" means even higher saving and lower consumption (either by government or by individuals) than is needed simply to deal with baby-boomer retirements.

Since Mr Bush has ruled out raising payroll taxes or cutting benefits for existing retirees and those near retirement, the options include cutting future benefits for younger workers (which could be done indirectly by raising the retirement age); mandating new individual saving; or borrowing the money, and implicitly raising the taxes of future generations.

Since Mr Bush has stipulated that the individual accounts must be voluntary, the reform cannot be based on forcing additional saving by today's workers. And since he has just pushed a large tax cut through Congress, whose costs balloon just as the baby-boomers start to retire, the government is unlikely to build up surpluses (ie, savings) outside the Social Security trust fund to help finance part of the transition. Both factors mean future benefit cuts and/or tax hikes will need to be larger than they might otherwise have been. A good test of the honesty of the commission will be whether it hesitates to point this out.

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Air-traffic control

Let pilots do it

Jun 7th 2001
From The Economist print edition

Satellites are at the heart of plans to improve air-traffic control

AROUND this time of year, Americans are usually braced for bad news about air travel. One group or another of pilots or cabin attendants is bound to announce plans for a strike that will leave them sitting for hours at the airport. Bad weather will stop the planes leaving; this accounts for half of the hold-ups. But the overriding problem is sheer congestion. Airlines schedule far more flights for a given time than can possibly be squeezed on to the runways. The real cause is the volume of air traffic, and an air-traffic-control system not good enough to handle it.

On any given day 1.9m Americans take off (God willing) on one of the 38,000 flights the airlines operate. In ten years, the figure will be nearly 3m. Yet nearly half of all flights at big airports arrive late. Two-thirds of all traffic goes through 31 hub airports, which account for 90% of delays. The worst are listed in our table.

On June 6th, the Federal Aviation Administration (FAA) unveiled what it thinks could be the remedy—new technology which will let pilots, as well as air-traffic controllers, make some of the decisions about where to fly. This will allow airlines to cram more planes into the same airspace. In conjunction with airport expansion, the FAA hopes, this could reduce congestion enough to let more people take to the skies without constant delays.

The naughtiest nine
Flight delays

Airport	Rate*	Average minutes late
New York, La Guardia	42	26.4
San Francisco, Intl	35	21.9
Boston, Logan	33	19.6
Chicago, O'Hare	33	20.0
Los Angeles, Intl	30	16.3
Philadelphia, Intl	30	16.9
Newark, Intl	29	18.0
New York, Kennedy	29	16.8
Atlanta, Hartsfield	27	15.4

*% of scheduled arrivals more than 15 minutes late
Source: FAA

The FAA's plan, which will be spread over ten years and will cost $11.5 billion, is mostly just an attempt to pull into one coherent whole a lot of projects that are already under way. There will be goals and deadlines. There will be two new runways this year, at Detroit and Denver; a further six by 2004 at another batch of congested airports, including Houston and Minneapolis; and yet another six by 2010 (at, among other places, Atlanta and Dallas). As well as covering green fields with tarmac, the FAA is to develop techniques for using them more intensively, speeding up the rate of landings and departures.

But the best hope for improving matters in the short term is to make air-traffic control faster and slicker. The worst problems occur during the thunderstorms of spring and summer; aircraft have to fly around storms, which means clogged air lanes. The FAA is working with NASA to find ways of forecasting storms with precision up to five hours ahead, and controllers are all to get computers on their desks to plot the best diversion instantly. Better traffic control would also allow aircraft in good weather to fly closer together than the five-mile lateral or 1,000-foot vertical separation that is considered essential today. To do so, however, they would need more accurate information about an aircraft's precise position, because many of the radar installations in use today are accurate only to within a mile or so.

Just a little closer

The FAA's answer is to make more use of satellites. Satellite-based data links will improve communication between pilots and ground controllers, cutting out about 40% of voice communication over the radio. As part of this, the FAA wants to phase in what is known as free flight—giving pilots more information about the position of other aircraft and allowing them to make more of the crucial traffic decisions. This does not mean leaving pilots free to steer their own course like car drivers, but it does transfer more responsibility for plotting a route and following it to the pilot, with the ground controller keeping an eye on things. The FAA plans to have a system whereby each aircraft in free flight has a

satellite-linked probe that tells the pilot if another aircraft is within 20 miles of him.

Other countries—especially those in Europe where the skies are even more crowded—will be watching the FAA's efforts closely. On the same day as the FAA declared its plans, Boeing announced the outlines of the future air-traffic-management system upon which much of the FAA plan depends. Boeing—which does not think the FAA's plan goes anywhere near far enough—reckons its system could cut today's delays nearly in half and, in future, do even better. Tensions between the company and the FAA may rise. For now the regulator is pleased that any private-sector firms have got involved at all, to help overhaul the system before it grinds to a halt.

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Peru's election

Toledo reaches the palace, at last

Jun 7th 2001 | LIMA
From The Economist print edition

EPA

If he is to rebuild democracy and revive the economy, the new president will need to form a credible government

Get article background

SAME man, same place, but what a difference a year can make. In April last year Alejandro Toledo stood on the balcony of the Sheraton Hotel in the centre of Lima, with a red bandanna round his head, and yelled to a seething crowd of supporters that President Alberto Fujimori had just stolen an election victory from him. Mounted on the shoulders of pro- democracy protesters, Mr Toledo then led a march on the presidential palace, only to be turned back by a wall of tear-gas.

Last Sunday night Mr Toledo was back on the same balcony, wearing a grey suit and glasses, having just become Peru's president with a narrow victory in a run-off ballot. He won 45.7% of the total vote, against 40.6% for Alan Garcia, a former president from the populist APRA party.

A lot has changed already in Peru since Mr Fujimori, beset by corruption scandals, sneaked out of the country last November. The electoral authority is now independent, for example. The vote was said by observers to be possibly the cleanest in Peru's history. But Mr Toledo, a centrist economist, still faces a daunting task if he is to make Peru, as he pledged to the crowd last Sunday, "a fairer country, with more jobs, without corruption, with more justice and equality for all."

The immediate task for Mr Toledo is to strengthen his political position. Many Peruvians voted against Mr Garcia, rather than for Mr Toledo. A last-minute fear that Mr Garcia might win appears to have caused many of those whom pollsters had thought might cast blank or spoilt ballots to back his opponent. Invalid ballots totalled 14%, in line with recent elections.

The new president lacks experience of government, and his authority has been undermined and his psyche scarred by allegations about his private life during the campaign. His Peru Posible party is a recently-created catch-all movement of individuals from the left and centre, lacking ideology and roots. It has only 45 of the 120 seats in Congress, though Mr Toledo claims to have struck alliances with three other parties with a total of 15 seats, and to be holding talks with two parties commanding another ten seats.

The importance of a team

These weaknesses mean that Mr Toledo's choice of ministers is crucial to inject credibility into his government. That is his first problem. Mr Toledo's chief economic adviser is Pedro Pablo Kuczynski, an experienced former energy minister and fund manager, who leads a team of technocrats. Investors hope,

and expect, that he will be named as both economy minister and cabinet chief. But Mr Toledo also faces demands for cabinet jobs from several of his political friends.

A formidable job for his government is to rebuild democratic institutions undermined by Mr Fujimori's ten years of elected authoritarianism. Here Mr Toledo has one advantage. The armed forces have been weakened by their entanglement with Vladimiro Montesinos, Mr Fujimori's disgraced head of intelligence. Four military chiefs are in jail, facing corruption charges. But several of their cronies remain in uniform. If Mr Toledo does not act firmly to clean up and rein in the army, the risk will remain that it will eventually step in, as it so often has when civilian governments have faltered.

Then there is the economy. After three years of near-stagnation, in the first four months of this year GDP contracted by 2% compared with the same period last year, according to the Central Bank. Investment, employment and earnings have all sunk from their levels of 1997. Despite rapid growth in the mid-1990s, GDP per person, in real terms, at $2,350 last year, is no higher than in 1970. Only around 40% of the workforce has a proper job; 54% of Peruvians are officially classified as poor. "People are desperate. It's a country facing a social emergency," says Elmer Cuba of Macroconsult, an economic consultancy.

During the campaign, Mr Toledo tried to match Mr Garcia's populist promises, vowing to double teachers' wages and to create 2.5m jobs over five years, partly through an emergency employment programme costing $170m a year. Finding the cash will be hard, given Mr Toledo's promises to maintain economic stability and honour the foreign debt. First, he must get the economy moving again. He has said he would cut sales tax and a special payroll tax. But that will prompt investment only if it is seen as part of a credible overall plan, argues Mr Cuba.

With his eye on Peru's social problems, Mr Toledo has pledged to reform the structure of government spending, raising education's share to 30% of the budget. He also wants decentralisation: local government currently spends only 4% of the budget.

There is scope for the new government to strike deals to its left on constitutional and social reform, and to its right on the economy. But that might require greater political skill than Mr Toledo has so far demonstrated. Should he stumble, he faces a powerful potential opponent in Mr Garcia, a far wilier and more experienced politician. Having returned to Peru only in January after eight years abroad, Mr Garcia has staged a remarkable comeback, and will have his sights on the presidency in 2006. He has offered his support to Mr Toledo, but in practice APRA's 28 congressmen are unlikely to give blanket approval to government measures.

Real change will take decades. After the turmoil of the past two years, Peru needs reform, but also steady, honest government. If Mr Toledo can deliver that, at least he will have pointed his country in the right direction.

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Politics in Ecuador

El loco's own goal

Jun 7th 2001 | QUITO
From The Economist print edition

A former president may survive a football scandal

ABDALA BUCARAM must have been relieved when a late goal gave Ecuador's football team victory over Peru in a World Cup qualifying match on June 2nd. Mr Bucaram, in voluntary exile in Panama since being ousted as Ecuador's president for "mental incapacity" in 1997, plans a political comeback. And a footballing defeat might have been fatal for his hopes.

That is because Mr Bucaram's supporters are alleged to have been behind an attack last month on Hernan Dario Gomez, a Colombian coach who has become a national hero in Ecuador by taking its lowly team to the brink of an unprecedented place in the World Cup finals. Mr Gomez had refused to include Mr Bucaram's youngest son, a mediocre footballer, in Ecuador's under-21 team. According to witnesses, the former president's elder son was one of a group of people who accosted Mr Gomez in the restaurant of his hotel in the coastal city of Guayaquil, shooting him in the leg and breaking his nose. Mr Gomez resigned, only to relent.

Mr Bucaram has long been known as *el loco* (the crazy one). But his hopes of a comeback may not be delusions. His Ecuadorean Roldosista Party (PRE) is still the third-largest in the Congress. At a conference in Panama last month, the party named him as its presidential candidate for the election due next year.

Mr Bucaram's resilience stems from his powerful political machine in Guayaquil. The grandson of Arab immigrants, he has never been accepted by Ecuador's traditional political elite—which strengthens his appeal among the poor. His six-month government was scandalously corrupt, but that is not unusual in Ecuador. On June 6th the president of the country's Congress resigned over corruption claims (which he rejects).

Mr Bucaram told his party's conference that there were no "barriers" to his returning to Ecuador to campaign. He still faces corruption charges. But it is said in Quito that the PRE may have struck a deal: in return for backing a two-point increase in VAT required by the IMF, the PRE expects government support for a measure to force Supreme Court judges to retire at 65. That would open the way for their successors to drop the charges against Mr Bucaram.

If Ecuador's footballers fail, an outraged public might cry foul at any such deal. But if they qualify, *el loco* might sneak back—and even win.

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Colombia's wars

Progress, of sorts

Jun 7th 2001 | BOGOTA
From The Economist print edition

The peace process produces a modest agreement

AFTER 30 fruitless months, peace talks between President Andres Pastrana's government and the guerrillas of the Revolutionary Armed Forces of Colombia (FARC) have produced a minor but tangible result. On June 5th, in an isolated spot in the mountains south-west of Bogota, the capital, the guerrillas handed over to the International Red Cross an injured police colonel and three other officers whom they had been holding captive.

EPA

Release for Acosta

They were the first of 42 imprisoned police and soldiers due to be released under a humanitarian accord signed three days earlier. In return, the government will hand over 15 sick guerrilla prisoners, but without dropping charges against them. The plan is that the FARC will then unilaterally release a further 100 of the 450 or so soldiers and policemen it is holding in primitive prison camps.

Military chiefs and some right-wing politicians have criticised the accord as premature, since the FARC has yet to agree to a ceasefire. Others have welcomed it, on humanitarian grounds. Alvaro Acosta, the released colonel, was disabled when the FARC shot down his helicopter. He was a symbol of the suffering of the captives and their families.

Certainly, both Mr Pastrana and his peace process needed some good news. As he nears the final year of his term, his popularity rating is languishing at 24%, while just 19% approve of his handling of the peace talks, according to a recent poll. That is likely to change only if the FARC shows signs of ending its war.

On another front, the government may also have achieved progress of a kind. It has been under foreign pressure, especially from the United States, from which it receives military aid, to curb the right-wing paramilitaries of the United Self-Defence Forces of Colombia (AUC). After several especially brutal massacres of civilians by the AUC, which claims 8,000 troops, the government has begun to take firmer action against it. Over the past two months, the security forces have arrested more than 60 AUC members, including several leaders. In a search for evidence against its financiers, investigators from the attorney-general's office raided the houses of several ranchers in the department of Cordoba, the AUC's heartland in north-western Colombia.

This pressure may be having an effect. Last week, the AUC's website carried a brief message in which Carlos Castaño, the AUC's founder, stated that he was resigning as its leader. After a meeting of its senior members, on June 6th the AUC issued a statement saying that Mr Castaño would retain joint "political control" of the AUC with another paramilitary leader, but would no longer form part of the organisation's nine-man "general staff".

It is thought that Mr Castaño opposed plans by other paramilitary commanders to turn their weapons on the security forces when pursued by them. That is something the AUC has hitherto made a point of not doing, since it claims to be an ally of the state (even if an increasingly unwelcome one) against the guerrillas. In their statement, the AUC leaders ratified their "respect" for the state, while criticising Mr Pastrana's peace policies.

Another factor in the AUC's apparent internal strife may be that the FARC has recently re-entered parts of Cordoba that had been under paramilitary control for the past five years. Last month the guerrillas visited several villages in Tierralta, in western Cordoba, rounding up civilians and then killing at least 11—perhaps as many as 80—with machetes in a deliberate act of terror. Opium poppies and coca are both grown in the area, which straddles a smuggling route for drugs and arms.

Since the start of talks, the FARC has cited the government's failure to curb the paramilitaries as a reason for its own failure to make peace. Coincidentally or not, the guerrillas signed the "humanitarian" accord in the same week as cracks appeared in the AUC—and just as their own behaviour in Tierralta showed as little respect for humanity as that of their paramilitary opponents.

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Argentina's economy

Cavallo pawns an uncertain future

Jun 7th 2001 | BUENOS AIRES
From The Economist print edition

Unless the economy rapidly returns to growth, a huge bond swap will have merely postponed a debt default

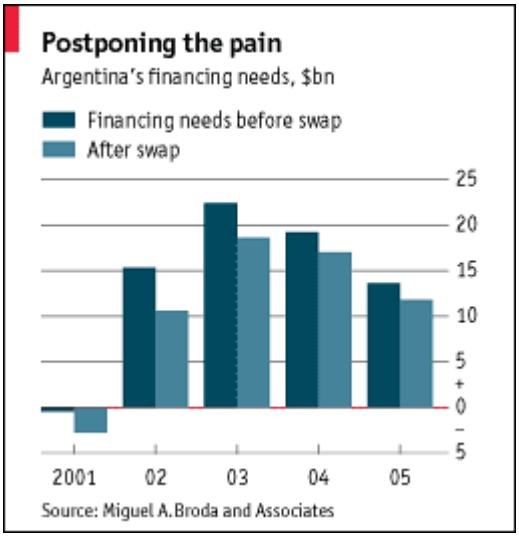
Get article background

"WE HAVE dealt with the urgent thing so we can dedicate ourselves to the important thing," declared Domingo Cavallo, Argentina's economy minister, last weekend, on concluding the biggest-ever voluntary refinancing of its debts by a government. This involved exchanging some $29.5 billion in mainly short-term debt for newly issued bonds which expire after 2005.

The urgent thing was that, before the swap, Argentina had looked unable to refinance the heavy burden of debt due to expire in the next five years and would, perhaps sooner rather than later, have defaulted. The important thing now is for Argentina's economy to grow, and fast.

After three years of recession, and with unemployment at 15%, depressed Argentines are desperate for a recovery. The swap aims to foster this by deferring some $7.7 billion in debt payments due before the end of next year, according to calculations by Miguel Broda, an Argentine economic consultant (see chart). Officials hope that this will lower short-term borrowing rates—for the government, but also for firms and consumers. In recent months, Argentina's borrowing bill has surged, as investors have demanded ever-higher premiums to compensate for the risk of default. The risk premium fell this week as investors gave an initial cautious welcome to the swap, whose scale exceeded most expectations.

But Argentina's reprieve has come at a high price. It will pay interest of about 15% on the new bonds, compared with an average of 9-12% on those traded in. The swap will be a success only if the economy returns swiftly to growth of at least 5% a year, and the government generates a fiscal surplus, thus reassuring investors that Argentina can service its postponed—and now augmented—debts in future.



There is no easy route to this. Argentina has not been able to kick-start the economy by letting its currency plunge, as Brazil did in 1999. By law, Argentina's peso is pegged at par to the dollar. Congress is discussing a proposal from Mr Cavallo to tie the peso half to the dollar and half to the euro—but only when (or if) the euro itself reaches parity with the dollar. Since most of Argentina's public and private debt is in dollars, a devaluation might anyway involve a default. Instead, Mr Cavallo's team promises sweeping reforms to bolster the public finances and improve the competitiveness of Argentine business.

The prospects, however, do not look good. Last December President Fernando de la Rua's government hoped that it had created the conditions for recovery by negotiating a $40 billion bundle of loans and credit guarantees, led by the IMF. But as the slump continued, in March investors and Mr de la Rua both panicked. The president changed his economy minister twice, turning in desperation to Mr Cavallo, a political opponent, who had held the job from 1991 to 1996.

Mr Cavallo has since announced measures to reactivate the economy and curb the fiscal deficit. After months of decline, tax revenues increased last month, thanks mainly to a new tax on financial transactions, copied from a similar measure in Brazil. But the government's attempts to reform pensions and health care are being held up by legal challenges. And, as Rosendo Fraga, a political analyst, points out, Mr Cavallo cannot get his hands on some of the most inefficient and corrupt government agencies, such as those for tax collection and social security. These are controlled by allies of Raul Alfonsin, a

former president who is the leader of Mr de la Rua's centre-left Radicals.

The finances of Argentina's provinces remain parlous: in the first quarter of this year, they overshot the government's target for their combined deficit by 12%. The economy ministry is refinancing the debts of those provinces that are ready to agree to a fiscal adjustment programme. But there is no sign of a structural reform of provincial finance.

Political clouds

With an election for Congress due in October, the prospects for unpopular reforms will not quickly brighten. A further complication involves a judicial investigation into the alleged smuggling of arms during Carlos Menem's first term as president in the early 1990s. Two close aides of Mr Menem's had already been arrested over the affair; this week they were joined by the former army commander. On June 7th, Mr Menem himself was placed under house arrest on the orders of the investigating judge. He still commands a wing of the opposition Peronists. His supporters had been pressing the government to intervene to prevent his arrest. They are now likely to make its life more difficult.

Above all, there is still no clear evidence that the economy is about to pull out of recession. Though industrial production is rising, consumer confidence remains low. Several months of political stability, fiscal reform and low interest rates could start to change that. But there is no guarantee that these will be forthcoming. And circumstances outside are not helping: growth in Brazil, Argentina's main export market, is set to slow sharply because of an electricity shortage, and the euro is languishing against the dollar.

Even after the swap, the government will still have debts to refinance in the next few years. Unless there is growth soon, Argentina's expensively acquired breathing-space may not last long.

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Nepal's week of horror

After the royal massacre

Jun 7th 2001 | KATMANDU
From The Economist print edition

AP

Can Nepal's fragile democracy survive the turmoil that has followed the slaughter of King Birendra and nine other members of the royal family?

Get article background

THE murder of a king and his family by his son, now that regicide has passed out of favour as a method of advancement, must be a profound shock to his subjects and a titillating horror to the rest of the world. For Nepalis, the killing of King Birendra and nine other members of the royal family on June 1st is that and something more: a reminder that a decade after the restoration of democracy Nepal is still unsettled about its form of government.

Nepal's elected government was widely despised before the murders. There is now a danger that the monarchy, regarded hitherto as untainted by politics and a unifier of a fissiparous country, may be also be loathed. Conceivably, one or both could be consumed by popular rage.

There are two sorts of ideas about what happened. The upmarket version is that the Eton-educated crown prince, Dipendra, enraged by his family's refusal to endorse his choice of bride, stormed into a gathering at the palace armed with at least one automatic weapon, slaughtered his family and then shot himself. He survived long enough to be named king, then died, leaving the throne to the murdered king's brother, Gyanendra.

The street version of events is very different. There are variations, some involving conspiracies by India or other foreign forces, but most suggest that the new king or his son, Paras, whose excesses have made him the least popular person in Nepal, was somehow behind the massacre. Several thousand people with that view took to the streets of the capital on June 4th. Three people were killed by police.

The government has three times imposed curfews. A fragile calm had returned to the city by June 6th. A committee appointed by King Gyanendra to investigate the massacre is supposed to report its findings in a few days. If the report is widely disbelieved, the streets could erupt again.

Nepal was unstable already. In 1990 King Birendra relinquished executive power and allowed multi-party democracy. As practised in Nepal, democracy has disappointed everyone. It has produced ten governments in as many years, many of them shaky coalitions. The current government of the centrist Nepali Congress Party has a big majority in the lower house of parliament but has ruled no more ably than its predecessors.

Factionalism has undermined its unity and corruption scandals have ruined its image. The main opposition party, the Communist Party of Nepal (Unified Marxist-Leninist) or UML, boycotted the last session of parliament, bringing normal government to a halt.

Only the Maoist insurgency seems to be gaining prestige rather than losing it. The Maoists control a half-dozen of Nepal's 75 districts, mostly in the impoverished hills, and swathes of some 25 others. Their style of government mixes enlightenment (they insist on girls going to school) and brutality. Some 1,700 people have died since their revolt began in 1996. They are now several thousand strong, but have potential sympathisers among the millions who do without education, electricity and decent wages. At least 40% of Nepal's 23m people live in poverty.

The massacre could change the relative strengths of the various Nepal power-seekers in unpredictable ways. The Maoists have, perhaps, the most to gain. Many detect their hand in the anti-Gyanendra protests. The Maoist leader, known as Chairman Prachendra, never a friend of the monarchy, has praised Birendra as a liberal, and by implication damned the new king as anything but. He may well be hoping that the investigation of the massacre will be seen as a whitewash, enraging people enough to welcome the Maoists down from the hills. If the masses storm the palace, the Maoists could conceivably take over.

Some democrats fear the palace itself. King Gyanendra, one of Nepal's most prominent businessmen, is thought to be decisive and hard-nosed, less like his brother in character than his father, who ended an earlier spell of democracy. This may be why some suspect him of wanting to put Nepal out of its democratic misery by restoring monarchical rule. Since the country's 50,000-strong army answers mainly to him, he has the means to do it.

The new king did his best to lay these fears to rest at his coronation by proclaiming his adherence to democracy and to constitutional monarchy. Even so, the fears were revived when the government ordered the arrest of the editor of a newspaper for publishing an article by a Maoist calling on the armed forces to revolt against the king.

Democracy will probably survive the crisis, but relations between king and government could change. Some people speculate that Gyanendra will try to make more assertive use than his brother of the powers the king retains, especially over the army and some aspects of foreign policy. Dipak Gyawali, a member of the Royal Nepal Academy of Science and Technology, thinks that he may be less reluctant to deploy the armed forces against the Maoist insurgency.

If the new king uses the army against the rebels without trampling on human rights, as the police have done, some think democracy might even gain. The Maoists have little incentive to negotiate with the government (they are demanding the resignation of the prime minister as their price). But they have taken part in elections before and might, faced with the army's muscle, be persuaded to do so again.

Nepal's stability depends most on how well democracy does its job. The current government may not deserve all the popular contempt it attracts. The economy grew a healthy 6.4% last year, and the government's economic reform programme is progressing reasonably well, considering the political problems the country has been facing. Yet cleaning up the banks and improving the civil service, vital as such reforms are, will not do Nepalis much immediate good. Reform is still much too slow, and is overshadowed by the corruption, cronyism and infighting that Nepalis have come to associate with democracy.

The next big test of the monarchy and, though less so, of democracy will come with the publication of the investigation into the royal massacre. The leader of the UML, Madhav Kumar Nepal, at first refused to join the three-man investigating committee, threatening its credibility and making politics look even more feeble than before. Mr Nepal has since decided to support the inquiry. The committee, which is headed by the chief justice and includes the speaker of the lower house, now looks as credible as any body investigating royal misdeeds can look. It is expected to name Dipendra as the killer. If people believe it, Nepal may return to normality under a new king. But for the long-term survival of Nepal's democracy, normality will not be good enough.

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Democracy in Central Asia

Don’t know, don’t care in Kazakhstan

Jun 7th 2001 | ASTANA
From The Economist print edition

Soviet habits linger on

EACH time a foreign politician of international renown passes through Kazakhstan, his country’s embassy wheels out some of the opposition to give the visitor a non-official account of the oppression and lack of democracy in the post-Soviet state—very much to the distress of the Kazakhstani government. The picture they paint is grim. The most recent dignitary to discover Kazakhstan was Germany’s foreign minister, Joschka Fischer. Of the eight opposition representatives he met in Astana, the capital, last month, four said that at some time they had been physically attacked. Most political parties in parliament, they told Mr Fischer, are artificial constructs set up as window-dressing for foreigners; most of the seats they occupy have been gained by election rigging. The independent media have been muzzled by the presidential family, whose members own 80% of all media outlets.

All this is true. But once the exercise is over and the visitor returns home, shuddering over what has become of Kazakhstan during its ten years of independence, another reality becomes clear. Most of Kazakhstan’s 14.9m people do not seem to care if they live in a democracy or not, have little interest in taking part in politics and support neither the government nor the opposition. In short, the people tend to be a passive lot, who prefer to be led rather than to find their own way, a taste described by one observer as the “apathy of society”.

But if indifference is so widespread, why does the government fear a few lonely voices of dissent? Viewed through western eyes, this behaviour may seem irrational. But those in power simply look at opposition, however minor, as a direct threat to their rule and to remaining in control. It may be a legacy of both the Soviet period and Kazakhstan’s earlier history when it was ruled by clans. “It’s bizarre,” says Eric Collings from the Organisation for Security and Co-operation in Europe. By law, simply criticising the president can be a violation of his honour and dignity.

After the discovery of an oilfield in the Caspian Sea last July that could turn Kazakhstan into a top producer, the Kazakhs believe that foreign businessmen will flock to their country irrespective of their political system. One sign of Kazakhstan’s greater assertiveness was the government’s very public rejection of the United States’ report on human rights earlier this year. The pro-presidential Civic Party slammed the report for being biased, discriminatory and tendentious in relation to Kazakhstan. That was not encouraging for the country’s small group of democrats.

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Idyllic Indonesia

An island to call your own

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From The Economist print edition

Choose from thousands

FANCY slipping away to a deserted tropical island? Indonesia has some 17,000 of them, all tropical and many uninhabited. It plans to offer a few to foreigners in a bid to drum up some much-needed cash.

One of President Abdurrahman Wahid's first acts on taking office 19 months ago was to create a new ministry to deal with sea resources. Its department for small islands has already had enquiries from, among other countries, Japan and the Netherlands, two former colonisers. Some come from companies seeking to exploit the islands commercially, some from rich westerners fancying a Robinson Crusoe life, preferably with luxury refinements.

Before allowing foreigners ashore on the sandy beaches, the government has to consider the possible problems that may ensue. Some of the most idyllic areas, for example the Moluccas, are beset with fighting. In 1999 several members of a family of Dutch descent were murdered during communal unrest in the islands. Some places, such as the Riau islands to the south of Singapore, are needed for defence.

National sovereignty is a touchy issue. Nationalist Indonesians are unhappy about leasing out parts of the country to the foreigners their fathers and grandfathers fought to oust in the 1940s. Their voice is likely to be stronger if the nationalist vice-president, Megawati Sukarnoputri, takes charge later this year, as expected. Officials in the maritime ministry now talk of managing the islands, rather than leasing them, although in practical terms there may be little difference.

Management contracts will be largely handled by regional governments, their powers enhanced earlier this year through regional-autonomy legislation. This should protect the rights of the local people. Contracts are likely to be for a few years at a time, but the length, terms and prices may vary from place to place.

What about the environment? Any potentially destructive activity, such as mining, is likely to be prohibited. Nevertheless, keeping the islands idyllic could be a problem. Indonesia has a good environmental law designed to protect its rainforests and has created marine parks to guard its coral reefs. But that has done little to prevent its rainforests going up in smoke and its reefs being destroyed by fishermen using bombs.

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Japanese politics

Problems of success

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Winning elections could make Junichiro Koizumi's task harder

WILL Junichiro Koizumi do the double? Talk that Japan's prime minister may call a snap election for parliament's lower house at the same time as the upper-house poll in July will not die away. The odds ought to favour a double election: opinion polls suggest that Mr Koizumi's reform-minded cabinet enjoys the support of almost every voter in Japan. Yet Mr Koizumi's position is unusual. A victory for his party, the Liberal Democrats (LDP), might hurt his cause, not help it.

Mr Koizumi is, of course, wrestling with the old problem of Japan's muddled party politics. Some of the most ardent supporters of his reforms, which centre on smaller, more open government and a reinvigorated private sector, sit on the opposition benches. His biggest enemies, on the other hand, lie within his own party. Already, Mr Koizumi's push to shrink Japan's bloated road-building budget has met with howls of protest from the LDP's road tribe, a group of political neanderthals who dedicate themselves to the grubby, money-soaked business of paving the countryside with asphalt. From the opposition benches, meanwhile, comes hardly a murmur of dissent. For all his popularity with the public, Mr Koizumi lacks the support within the LDP's parliamentary party to take on the likes of the road tribe in an open fight. So some of his supporters are urging him to go to the voters, and return with a stronger mandate for reform. Yet it is the fear of what might happen at the polls that helps to keep Mr Koizumi's enemies in the LDP in check. They do not attack him openly. Instead, they snipe at his foreign minister, the redoubtable Makiko Tanaka, a woman whose outspokenness is unsettling those who prefer Japan's usual ultra-cautious diplomacy.

With the lower-house election out of the way, however, Mr Koizumi himself could become fair game. In fact, it may be the upper-house election, scheduled for July 29th, that offers Mr Koizumi his biggest chance to shake up Japanese politics. The opposition parties have pinned all their hopes on winning this election. Yukio Hatoyama, leader of the Democratic Party, the biggest of the opposition forces, says he will use control of the upper house to block legislation and so force an early general election. But Mr Koizumi's extraordinary popularity has thrown Mr Hatoyama's plans into disarray.

If the Democrats lose at July's polls, they have nowhere to go. Except, perhaps, into government. Since taking office in April, Mr Koizumi has been careful not to rule out co-operating with the Democrats, even hinting, from time to time, that he would welcome it. If Mr Hatoyama did join hands with Mr Koizumi, the Democrats would undoubtedly split. A large minority, descendants of old cold-war socialists, would never brook Mr Koizumi's calls for more active defence forces. Yet the party might split anyway. A few younger Democrats have openly voiced their support for Mr Koizumi, and many more admire him in private.

With more reformers in government, meanwhile, the LDP's road tribe and other cavemen may be encouraged to go. The cabinet's supporters in government and its enemies in opposition—a novel thought for Japan, but not an entirely foolish one.

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Chinese-American relations

More sound than fury

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From The Economist print edition

China keeps its anger under control

Reuters

Hegemonism? Who cares?

THE United States and Taiwan be warned. According to China's state-controlled media, thousands of troops are massing on a holiday island in the Taiwan Strait for one of the country's biggest war games, codenamed Liberation One. Their mission: to demonstrate that China is quite capable of defeating Taiwan militarily, even if the Americans try to protect it. The island of Dongshan, close to the Chinese coast, where the manoeuvres are being held, is said by the Chinese press to be just the spot for such a display of prowess. Its topographical features are similar to those of Taiwan itself.

The Chinese media have tried to drive the point home by highlighting some of the sophisticated weaponry being deployed on and around Dongshan (home to 200,000 people and famous for its asparagus). There will be Russian-made Su-27 fighter jets, submarines, amphibious tanks and advanced missiles. The state-run China News Service has published a photograph of Chinese soldiers standing round a large relief map of Taiwan as if studying its vulnerabilities. The *Beijing Morning Post* has reported that the Dongshan exercise would practise seizing Taiwan's offshore islands and attacking aircraft carriers.

Given China's anger over what it sees as a series of provocations by the United States and Taiwan, sabre-rattling such as this is the kind of response that might have been expected. In 1996 China also launched war games around Dongshan to make clear its fury with the Americans for allowing the then Taiwanese president, Lee Teng-hui, to pay a visit, and with Mr Lee for singing the praises of Taiwan's democracy during his trip.

This time China is angry with the United States for allowing President Chen Shui-bian of Taiwan to meet senior American politicians in New York and Houston on his way to and from a visit to Latin America. To make matters worse, President George Bush received the Dalai Lama at the White House around the same time, treating him as a respected visitor, instead of dropping in on a meeting with another official, as Bill Clinton used to do to avoid riling the Chinese. All this as China was still smarting from the spy-plane incident in April, as well as President Bush's decision to allow the biggest sale of arms to Taiwan in nearly a decade and press ahead with a missile-defence system that the Chinese say could destroy international arms-control efforts.

But China is not in a mood to take the Americans on. Chinese spokesmen are being considerably more guarded than are the official media in their comments on the war games. Indeed, the Foreign Ministry in Beijing has been sounding rather like the Taiwanese and American governments, which have both portrayed Liberation One as a routine annual drill that is nothing to worry about. Don't confuse it with other issues, says a spokesman, Sun Yuxi. Senior officials have privately criticised the editors at the *Beijing Morning Post* for their reporting of the war games.

China has one obvious reason for refraining from more heated polemics, or the kind of dangerous heightening of tension it provoked in 1996 when it lobbed unarmed ballistic missiles close to Taiwan's two biggest ports. Last week Mr Bush decided to renew China's low-tariff trading rights with the United States for another year (or until China joins the World Trade Organisation, the WTO, after which it will permanently enjoy such rights). Announcing this, Mr Bush said his country had a huge stake in the

emergence of an economically open, politically stable and secure China. These are the kind of words the Chinese like to hear. They have long accused the Americans of trying to destabilise Communist rule by supporting anti- government groups. Mr Bush's remarks sounded as close to an acceptance of the political status quo in China as any American leader is likely to utter.

China wants American acceptance badly. President Jiang Zemin was delighted by Mr Clinton's visit in 1998 and the opportunity it afforded him to show his citizens that China was no longer shunned by the world's most powerful nation. Mr Bush is due to visit Beijing after taking part in a summit of Asian and Pacific leaders in Shanghai in October. The Bush visit will change the tone of the relationship for the better, says Chu Shulong, a senior research fellow at the state-sponsored China Institute of Contemporary International Relations.

China does not want to ruin its chances by appearing too belligerent

Also constraining the Chinese is their burning desire to hold the Olympic Games in 2008 (for reasons of prestige as much as any enthusiasm for sport). The International Olympic Committee will announce the winning city in July. China does not want to ruin its chances by appearing too belligerent. The Chinese have forced the Americans to agree that their spy plane, still stranded on Hainan Island, will be chopped up and flown out by transport aircraft rather than repaired and flown out in one piece. They have also refused to allow an American minesweeper to pay a routine visit to Hong Kong. But these are minor punishments, given the scale of America's alleged transgressions.

Indeed, the atmosphere seemed quite friendly this week in Shanghai at the meeting of the United States' trade representative, Robert Zoellick, and his Chinese counterpart, Shi Guangsheng. There was no obvious sign of progress in their discussions about China's bid to join the WTO, but that is unlikely to be related to recent tensions. China's unwillingness to give further ground on such issues as agricultural subsidies is more to do with domestic considerations. The Communist Party's powerful Organisation Department has just published a hard-hitting study of unrest in China. It says that WTO entry could have a serious impact on social stability; the fear is that the big protests about economic grievances that already take place will rise in number.

Many in China are unhappy with the government's stance. Internet bulletin boards in China are full of messages saying the leadership should attack Taiwan rather than waste time with exercises. People are against the government's soft policy towards Taiwan. This undermines stability, says Yan Xuetong, of Qinghua University in Beijing. But the leadership clearly reckons that giving vent to public anger would be even more destabilising than suppressing it. With sweeping changes at the top planned for next year and the impact of WTO entry to worry about, the authorities would prefer not to add confrontation with America to their list of anxieties.

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The EU's summit in Gothenburg

Enlargement ahoy?

Jun 7th 2001 | BRUSSELS
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The Swedes may have managed to nudge negotiations to bring eastern newcomers into the EU further than expected

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The EU's Prodi and Persson, big enlargers

THE Gothenburg summit of the European Union that starts on June 14th is being viewed by its Swedish hosts with excitement tinged with a faint sense of foreboding. After their six months of presiding over the EU and setting its agenda, the Swedes can point to some solid progress in the area they have chosen to emphasise: the negotiations to bring as many as a dozen new members into the Union. They will also have the honour of playing host to the first summit between the EU and the United States since George Bush became president (see article).

But the presence of so many heads of state will also mean hordes of demonstrators—greens, anarchists, socialists—descending on Gothenburg. To the Swedes, who pride themselves on informality and openness, this presents a dilemma. "The last thing we want to do", says an official, "is seal the city off and disappear into a bunker." In a perhaps quixotic attempt to head off trouble, Goran Persson, Sweden's prime minister, will meet the protesters the day before his VIP guests arrive.

The Swedes may not be able to ward off disorder on the streets. But events in the conference chamber may be a lot calmer than seemed likely a couple of weeks ago. That is because a looming row over EU enlargement has been put off, at least for a while. The Union's enlargement negotiations are beginning to touch on some of the most sensitive issues. How soon, for instance, will Poles and others automatically be allowed to work in the West? How quickly will westerners be allowed to buy land in the countries that join? How fast will the EU switch its regional aid from countries like Spain and Portugal to the poorer newcomers?

In the approach to the Gothenburg meeting, the Spaniards were threatening to prevent the EU from adopting a common position on the free movement of labour in an enlarged EU unless they got guarantees about regional aid. But vehement objections from other EU countries caused the Spaniards to back off. They will no longer block the EU's proposals, made in deference to German and Austrian fears of being flooded by cheap labour from the east, to impose a transition period of up to seven years on the newcomers before completely free movement of labour is allowed within an enlarged Union.

The Spaniards have been fobbed off with the promise of a political declaration that "takes note" of their concern that enlargement, by lowering EU countries' average wealth, will disqualify most Spanish regions from aid programmes. The EU's 15 existing members are still haggling over the declaration's wording; the row could still flare up at Gothenburg. But, now that the link with the free movement of labour has been broken, the dispute is much less likely to get out of hand.

In the past fortnight another tricky problem to do with enlargement has come closer to resolution: sales of land. Many of the applicant countries are worried that when they join the EU rich foreigners will come in and buy up large tracts. This obvious echo of the Austro-German fear of cheap labour from the east has led the EU to make a symmetrical offer: to allow a seven-year pause before the new countries are obliged to let anyone from anywhere, including big western agri-businesses, buy up their land.

Rather to the surprise of the existing EU members, the Czechs have already shaken hands on this proposal, though the Poles and Hungarians are still unhappy. Indeed, there is a growing feeling that the Poles, hamstrung in part by a general election expected in the autumn, are slightly flagging in the race to get into the club.

So the Swedes can justly feel that they have made good on their aim to crack on with the enlargement negotiations. They are particularly pleased with progress on another awkward topic—the environment—which will entail the candidates making costly changes to comply with strict EU rules. Despite worries that this would be a sticking-point, deals have already been struck with Hungary, Slovenia, the Czech Republic and Estonia.

When's the magic day, then?

The Swedes hope to crown their success at Gothenburg by setting a firm date for concluding the entry procedure. This has been a long-standing demand of the candidates, who fear that otherwise they may get sucked into a never-ending tunnel. But the EU's negotiators in Brussels reckon that trying to set a firm date could be a mistake: it could lock the EU into a promise it regrets, prompt new fights among the existing members, and risk taking pressure off the applicants. The Swedes, however, remain hopeful. "Political leaders may be capable of a bold declaration that professional negotiators can't make," says one of those involved.

Still, though the summit is likely to concentrate on enlargement, with nods at environmental and social issues, there is always a chance that other matters—more violence in the Middle East, for instance—may intrude. If the Irish in their referendum on June 7th were to have unexpectedly rejected the Nice treaty so painfully negotiated at the EU's grand summit last December, Europe's leaders would have a horrible problem on their hands. If Tony Blair were to have lost the British general election on the same day, Europe's leaders would face a recalcitrant new British prime minister in the form of William Hague. And there is always the possibility of a squadron of pigs flying over the Swedish conference hall.

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Restitution in Poland and the Czech Republic

Muddy water

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Poland and the Czech Republic are still struggling with unresolved claims for property restitution

MORE than ten years after the end of communism in Central Europe, the restitution of property grabbed after the second world war is still a hot potato among Czechs and Poles. The Czech government is at odds with the Roman Catholic church, which has been trying to get back over 200,000 hectares (770 square miles) of land. Earlier this year the Poles' sickly right-wing government at last passed a restitution bill, but the country's ex-communist president, Alexander Kwasniewski, vetoed it in March.

Unsurprisingly, many claimants to property in Poland have run out of patience and taken their cases to court, both in Poland and America. A National Coalition of Organisations for Restitution may be planning to bring as many as 40,000 cases to Polish courts. Jewish claimants are having a class-action suit against the Polish government heard in New York—and have lobbied hard to get George Bush, the American president, to bring up the thorny topic when he meets Mr Kwasniewski next week.

Outstanding restitution claims have come back to bug the Czech and Polish governments because foreigners in particular are wary of investing in property whose ownership is uncertain. The Czechs are in less of a muddle, as their government passed restitution laws some ten years ago, when the country was part of Czechoslovakia. But the Poles still have no laws governing the return of private property. It remains unclear, for instance, who owns many buildings in Warsaw. Indeed, a family of Poles claims the land on which the American embassy sits.

The first round of confiscation in Czechoslovakia began within months of the war's end, in 1945, under laws pushed through by a non-communist president, Edvard Benes. The Benes decrees, as they were called, were aimed particularly at the country's 3m Sudeten Germans, many of whom had cheered the Nazi invasion in 1938. When the Communists ousted Benes in 1948, they nationalised vast swathes of the economy with another batch of laws that went much further.

In 1990 and 1991, after the "velvet revolution" had ended communism in Czechoslovakia, the new government passed laws on restitution. But their generosity was limited. Only those who still held a Czechoslovak passport and whose property had been confiscated between February 25th 1948 (the day the Communists took power) and January 1st 1990 could claim. That excluded Jews who had lost land or property after the Nazi invasion in 1938. It also ruled out Germans whose assets had been expropriated under the Benes decrees, even if they had never collaborated with the Nazis.

Moreover, the government set a tight deadline for the claims. Many of these aggrieved people have given up. Still, the government says that over 1.2m hectares of arable land, nearly a third of the country's total, has been given back to private owners. Claims had to be filed by May 25th, ten years after the law was promulgated; it will now be almost impossible for non-Czech citizens to reclaim property.

Polish restitution, for reasons of geography and history, is trickier still. The country's borders shifted several hundred kilometres west after the war. The Poles' former communist party, now revamped as a social democratic one, is again the strongest in the land. And, compared with the Czech claims, a much larger portion of claimants are Jewish.

The Koppenheim case illustrates the complexity. Peter Koppenheim, chairman of the Holocaust Restitution Trust in Britain, was born a German citizen in Breslau. He says that, among other property, a block of flats in the heart of what is now the Polish city of Wroclaw is his. In 1939 the Nazis forced his family to sell its property cheaply to Germans. After the war the communists nabbed it. The first post-communist government returned the block to the descendants of the German family, who then sold it to Thyssen, the German steelmaking company. Mr Koppenheim is one of the class-action claimants in the suit being heard in New York.

Despite Mr Kwasniewski's veto of the restitution bill, his government may well get more such suits. The bill he turned down might have cost the government $11.75 billion, compensating successful claimants to the tune of half the property's present value—provided they held a Polish passport. "Now we're going for 100% compensation," says Mr Koppenheim.

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France's prime minister

He just trotted along

Jun 7th 2001 | PARIS
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The revelations of Lionel Jospin's far-left past are less harmful than his previous efforts to cover it up

SHOCK, horror, hold the presses—or, rather, run more copies. It seems that Lionel Jospin, France's Socialist prime minister for the past four years, was once a member of a hardline Trotskyite movement, the Internationalist Communist Organisation (OCI). Worse still, his assigned role, as a student at the École Nationale d'Administration (ENA) that trains the country's governing elite, was to infiltrate the establishment. Worst of all, if his links with the Trotskyites, begun in the 1960s, really did last until 1987, he may have been an extremist mole within the Socialist Party, of which he was first secretary from 1981 to 1988. In other words, some may soon speculate, perhaps Mr Jospin is even now plotting to undermine France—second-biggest economy in the euro-zone, independent-minded pillar of NATO, permanent member of the UN Security Council, and so on—from within.

EPA

A younger Jospin, in denial

But back to a more mundane version of reality. Reacting to revelations by *Le Nouvel Observateur* and *Le Monde*, Mr Jospin (or "Michel", as he was known to his revolutionary comrades) told parliament on June 5th that he had indeed "formed links" with a Trotskyite group in the past, but it was "a matter of a personal journey, intellectual and political, of which I have nothing to be ashamed."

Fair enough. After all, there are plenty of generally respected politicians (think of Germany's foreign minister, Joschka Fischer) whose youthful enthusiasms pushed them to the far left. Indeed, Mr Fischer's politics involved him in street battles, in one of which he clobbered a policeman. Moreover, for Mr Jospin, son of left-wing parents, the Trotskyites doubtless seemed an honourable alternative both to the Socialists, tainted by their support for French colonialism, and to the Communists, blind to Russia's brutality at home and abroad. Boris Fraenkel, a stateless Jewish refugee who recruited Mr Jospin to the OCI, was just the sort of rigorous intellectual to appeal to Mr Jospin. As the prime minister told parliament, on his political journey he "met some remarkable men—which helped my education."

So is this week's furore merely silly-season froth? Not quite. In the past Mr Jospin has resolutely denied rumours of a Trotskyite past. In 1995 he told *Le Monde* that he had "never been a Trotskyite" and that the rumour-mongers were confusing him with his older brother, Olivier (codename "Camus"), a leading member of the OCI's central committee. So why the denial? Mr Jospin lamely explained to parliament this week that he thought it was no one else's business: having ideas and freedom of thought go together, "and I didn't see why I should have to render an account."

Perhaps the voters will agree, not least because the popular assumption is that all politicians lie. The problem for Mr Jospin, however, is that he has created a public image of honesty, and with only a year to go before the presidential election, in which he is set to oppose the conservative incumbent, Jacques Chirac, he can hardly afford to let that image be sullied. After all, an opinion poll taken just before Mr Jospin admitted to his Trotskyite past put him closely behind Mr Chirac—even though Mr Chirac's own image is more tarnished than most.

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Crisis in Berlin

All change?

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Berlin's city-state government is in a financial hole. An election? Probably

THE supposed dazzling showpiece of a newly self-confident united Germany, Berlin is sinking into a financial mire. Behind the resplendent façades of the new federal government buildings and gleaming commercial centres, the city's local government is staggering under spiralling debts, fleeing businesses, vanishing jobs and a property-market collapse. The long-awaited boom in the city, readopted as the national government's seat in 1999, has not arrived. And now the Social Democrats have decided to pull out of the Christian Democrat-led "grand coalition" that has ruled the city-state since 1991.

Berlin's economic growth is the lowest of any of Germany's 16 *Länder*. Its tax revenue, also the lowest per person, covers barely 40% of its spending. The rest has to be financed through handouts from the federal government, transfers from the richer states, privatisation and borrowing. Since Germany was united in 1990, the city government's debts have risen fivefold to DM65 billion ($28 billion), DM20,000 or so apiece for each of its 3.4m inhabitants—double the average for the other *Länder*. Interest payments gobble up a tenth of the city's DM40 billion annual budget. And public borrowing now looks set to leap another DM10 billion.

Less than a month after the official opening of Chancellor Gerhard Schröder's palatial new offices in the capital, costing a cool DM465m, Berlin's local political bosses were sent reeling by the revelation that Bankgesellschaft Berlin, the country's tenth-largest bank, in which the city has a 57% stake, was on the verge of collapse. Desperate to save the biggest non-government employer in a city where 16% of the workforce is jobless, the Christian Democratic mayor, Eberhard Diepgen, who had already planned to borrow DM4 billion to meet this year's budget deficit, has promised to borrow another DM6 billion to keep the bank afloat.

For some four decades after the second world war, West Berlin was an island of democracy in a communist sea. Its local administration lived happily off fat subsidies from the West German government in Bonn. These met half its spending. But after unification, they were drastically slimmed. Since the mid-1990s, a few local politicians have made valiant efforts to tidy up Berlin's chaotic accounts, cutting public spending, axing city-government jobs (down by a third since 1995) and selling property. But whenever a hiccup occurred, party bosses invariably went cap in hand to the federal government.

This year, no exception. The city's leaders plead that because of its past division, rich Prussian cultural heritage and renewed status as the national capital, Berlin has special needs. But the federal government, run since 1998 by Mr Schröder's Social Democrats, has at last had enough of bailing out a city dominated for all but two of the past 20 years by their main rivals; Berlin must put its own house in order.

The stench of political scandal, mismanagement and corruption that for years has dogged Berlin's Christian Democrats does little to stimulate sympathy or indulgence. Last month Klaus Landowsky, leader of their forces in the city-state's parliament, was obliged to step down. For a score of years he has been the power behind Mr Diepgen. But he had admitted to having accepted illegal donations to his party in the mid-1990s from two property developers who had been granted a loan worth DM600m by Berlin Hyp, a subsidiary of Bankgesellschaft Berlin headed at the time by Mr Landowsky himself. A criminal investigation is under way. But Mr Diepgen has continued to cling to his former *eminence grise*, getting him elected as deputy party chairman in the city.

So the Social Democrats have at last decided that enough is enough. For months, the opposition Greens, with whom they share power in the federal government, and the ex-communist Democratic Socialists, who scooped up 40% of the vote in formerly communist east Berlin in the last city elections in 1999, have been pressing them to pull out of the ruling coalition in Berlin, force an election, and fight it alongside them. At first, the Social Democrats resisted, fearing a repeat of the debacle in 1999, when their share of the vote collapsed to a post-war low of 22%. But faced with the Landowsky scandal, the

mounting financial crisis and the slide in support for the Christian Democrats, they are poised to take the plunge. Despite a last-ditch effort by Mr Diepgen to save his government with a new austerity package involving further spending cuts of DM800m, the Social Democrats on June 7th announced they were jumping ship. They want to see elections for a new Berlin assembly in September.

If current opinion polls hold good, the Social Democrats should then win enough votes to form a new coalition to run the city with the Greens and the Democratic Socialists. Mr Schröder no longer objects in principle to his party chumming up with the ex-communists; it has already done so in the eastern state of Mecklenburg-West Pomerania. Still, he would rather have avoided exposing himself to attack on that flank so soon before next year's general election.

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Simeon of Bulgaria

Jun 7th 2001
From The Economist print edition

Bulgaria's would-be ruler, one of Europe's resurgent royals

"TODAY I declare my goal: to found and lead a movement in the name of new ethics in politics, new economic decisions, new ideas and new leaders. With this address, I declare the birth of the Simeon II National Movement." At last, a moderniser for Bulgaria and its democracy: God save Simeon Borisov Saxe-Coburggotski! He declares himself worried by poverty in his country, and by the contrasting opulence of its leaders. His movement, set up in April, hopes, in alliance with a women's party, for "overwhelming" support in Bulgaria's general election on June 17th. But this bearded, Madrid-based businessman of 63, fond of brown jerseys and cigarillos, is not quite your average modern democrat. He is a king.

To be exact, an ex-king: unluckily for him, Bulgaria is a republic. Worse, he has spent little time in it. He left his then Soviet- satellite country at the age of nine, in flight first to Egypt, then to Spain (where he became, among other things, a pilot), making his first visit back only in 1996. Yet thousands of Bulgarians welcomed him. Earlier this year, however, the country's electoral commission torpedoed his plan to run for president: he had not lived long enough in Bulgaria. Indeed, the commission only grudgingly let his alliance field candidates in the general election: Bulgaria's Supreme Court had earlier ruled that the ex-king's control of his supporters was, well, too monarchical.

Even so, his movement, campaigning against corruption and favouring more privatisation, may yet have a sniff at power. A woman politician is in nominal charge, and Mr Borisov—as hard-left critics jeer at the late King Boris's son—avers that he wants accountable leaders. He denies any attempt to regain his throne: "At this historic moment, the only reason for me to be a leader is to work for the good of all in Bulgaria." Many believe him: his movement is far ahead, say the pollsters. One of them, a few weeks ago, found that 43% of voters would plump for it.

After Bulgaria, where next?

Royalist sentiment got a fillip last year when Russia's Orthodox church canonised the last tsar, Nicholas II, murdered by Bolsheviks in 1918. Now Bulgaria's regal emotions may encourage others—and there is quite a list of exiled royals from eastern and southern Europe. Romania's ex-king, Michael I, was sent packing by its first post-communist president, Ion Iliescu, when he tried to return in 1990. But his citizenship was restored in 1997 and Romania's Senate has agreed that he (and other ex-heads of state) should be paid a salary equal to half the president's, plus a residence and a special guard. Though his home is still in Switzerland, he recently visited his country again, at the invitation of Mr Iliescu, who won back the presidency last year.

Several other exiled royals have tried to edge their way home, making the most of their countries' renewed nationalism. Within days of Slobodan Milosevic's downfall last year, Yugoslavia's new leader, Vojislav Kostunica, had a visit from "Crown Prince" Alexander, a fervent supporter of his opposition movement. Like other returning royals, Alexander attracts welcoming crowds when he steps on home soil. And he too fancies a state role. During the Kosovo war, the heir to the former throne of Montenegro (Serbia's partner in what is left of Yugoslavia), Prince Nikola Petrovic-Njegos, a Paris architect, said he would like to go back to the royal palace in the former capital, Cetinje, if Montenegrins wanted him. Albanian royalists, too, can make a little noise. In April, on the 40th anniversary of the death of King Zog, family fans gathered in a Paris cemetery to condemn extremists and appeal for peace in Macedonia. Zog's son Leka, who lives in South Africa, still fancies getting the throne back.

Unseemly father, underwear, unwed mother, pot

Though monarchies will not be restored any time soon in the ex-communist east, any swing that way is in contrast to the rest of Europe. Two world wars, Lenin and then Stalin finished off many thrones.

Monarchs reign in only seven countries: Belgium, Britain, Denmark, the Netherlands, Norway, Spain and Sweden. Luxembourg has its grand duke, the mini-states of Liechtenstein and Monaco have princes. And doubts, in some, are growing.

Family rows and divorces have shaken the British throne for years. Dutch eyebrows were raised recently at Crown Prince Willem Alexander's plans to wed the daughter of a man who had been a minister (for agriculture) in Argentina in its days of military rule. Spaniards this spring were shocked by stories that Crown Prince Felipe had similar plans for a Norwegian model, no less, who, even worse, had posed in her underwear (in, not out of, it, but decent Spanish girls go clad head to foot in *chadors*, don't they?). The intended of Norway's Crown Prince Haakon is—wait for it—a single mother, and his sister goes out with a man who has smoked cannabis. Why, ask Norwegians, have a royal family if it behaves like an ordinary one? One poll suggests that half of them would like a referendum on the monarchy.

Nor will the republics go the other way. France's monarchists are, deservedly, a joke. Greece's ex-King Constantine, who fled after a coup in 1967, last year won a promise of compensation for his confiscated palaces, but no offer of his crown, abolished after a referendum in 1975. Italy's House of Savoy, booted out in 1946, is fighting a constitutional ban on any male member's return home. Italy's prime minister-elect, Silvio Berlusconi, hints that the Savoyards may be back soon, if they eschew politics.

The one weighty figure in this gallimaufry is Otto von Habsburg, heir (though not claimant) to a weighty ex-throne, that of Austro-Hungary. Now 88, this lifelong pan-European is a political scientist who was for many years, in Bavaria's interest, a Euro-MP. His elder son Karl has been a Euro-MP too—for Austria; his younger one, Georg, is a high-flying diplomat—for Hungary. With or without crowns on their head, once-or-future royals can do admirable things yet—as Mr Borisov hopes soon to prove.

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Serbia and Slobodan Milosevic

The noose tightens

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From The Economist print edition

The Serbian authorities may be preparing to send their former leader to face the UN's war-crimes tribunal at The Hague

EVEN by the unspeakable standards of recent Balkan history, it was grisly news. The Belgrade authorities said on June 3rd that investigators were examining scores of bodies from several mass graves at undisclosed places in Serbia. They were the corpses of civilians killed in Kosovo, stashed away to hide them from war-crimes probes.

Some of the bodies, apparently including those of women, children and old men, were recovered in April 1999 (as the war over Kosovo was in full swing) from a truck dumped in the Danube. Last month, Serbian police confirmed that around that time they got an order from Slobodan Milosevic, then Yugoslavia's president, to dispose of the corpses of civilians killed in cold blood.

Few people in Belgrade, the Serbian capital, have any doubt as to why these facts are coming out now. The authorities want to prepare public opinion for the eventual extradition of Mr Milosevic to the UN's war-crimes tribunal in The Hague. America wants some progress at least in that direction as the price of its attendance at a conference on aid to Serbia on June 29th. The autopsies have also served to concentrate the minds of a hardline Montenegrin party that shares power with reformist Serbs in Yugoslavia's shaky federal government—and feels protective of Mr Milosevic.

Vojislav Kostunica, the federal president and a reluctant convert to the need for co-operation with the Hague court, has been warning his Montenegrin partners that their obstructive tactics might prove to be the *coup de grâce* for the Yugoslav state, which now consists only of Serbia and Montenegro. That would be a historic irony, given that the Montenegrins in question speak for the pro-Serbian half of their tiny republic's divided electorate.

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Slovakia's populists

Snap and snarl

Jun 7th 2001 | BRATISLAVA
From The Economist print edition

Dogfights as this EU applicant prepares for an election

POPULISM is the name of today's game in Slovakian politics. Three populists are now muscling in on next year's general election, snapping and snarling at allegations of government corruption, which recently led the European Union to suspend, temporarily, some payments to Slovakia.

The most established of the three is Vladimir Meciar, the main inspirer of the break-up in 1993 of Czechoslovakia. He jeers at the fractious governing coalition of the centre-right, which was formed specifically to keep him out of office. But Slovaks recall how he drove the country into the ground during his years as prime minister from 1993 to 1998. Pollsters say 25% of the vote is the best he can hope for—not bad in itself, but he has no chance of building a solid coalition. Only the racist Slovak Nationalist Party, backed by about 8% of voters, wants anything to do with him.

What about Robert Fico, a slick 37-year-old who is now the country's most trusted politician? He is keen on law and order. Crime has exploded, he says, and he is just the man to bring the Gypsies, sorry, the criminals, to their knees. The headquarters of his party, Smer (Direction), attest to his common touch. They sit "where the real people are", in the heart of a working-class Bratislava housing estate. Inside, all is glossy and professional; Smer is a party run by the young for the young. Computers abound; Mr Fico reckons people on the net are the sort most likely to support him.

Few doubt his ability. He qualified as a lawyer at an early age, and represented Slovakia at the European Court of Human Rights in Strasbourg. Substance is another matter. In Communist days, he was a party member, but only, he says coldly, out of ambition. He split with the ruling coalition's socialist bit in 1999; nowadays, he is a pragmatist. He railed against NATO when it bombed Belgrade. Now, with the public mood towards the alliance softening, he is a NATO supporter. Opinion polls give Smer around 20%. If the election does the same, the present ruling coalition would need its support.

The price might be high. Mr Fico has made no secret of wanting to be prime minister. Nationalists see him as a possible ally. Mr Fico publicly dimisses this, but hints that ethnic-Hungarian parties would not be welcome in his government.

For those who like their populists rough and ready, there is a third contender, Pavol Rusko, a young television magnate with an admiration for Italy's new prime minister, Silvio Berlusconi. Mr Rusko built up TV Markiza, Slovakia's biggest station, with American money—proof, he says, that his allegedly close links to Russia are a myth. He got his start from Mr Meciar, but split with him the moment it became bad for business, and switched to backing the ruling coalition.

In April he launched his own party, Ano (Yes), with a chunk of his own money—though he promises not to use his television station to the same end. The pitch was a tired one: Slovakia's politics needs new faces, as long as they are Mr Rusko's pals in business and sport. He hopes to poach 10% of the vote from the ruling coalition, the nationalists and especially Mr Fico. But the professional politicians are running rings round him.

Such a professional is the prime minister, Mikulas Dzurinda. As he sees it, the populist vote is not growing but splintering. Anyway, he says, Messrs Fico and Rusko, both keen on EU membership, cannot be likened to authoritarian Mr Meciar. Too bad for Mr Dzurinda, then, that his own vote is splintering. Now the country's least-liked politician, he heads a party that scores barely 10% in the opinion polls.

Just proof that the government's painful reforms are working, Mr Dzurinda chirpily responds. There are indeed some hopeful signs: Slovakia was recently admitted to the OECD, the economy is growing, foreign investment is rising. But with unemployment stuck above 20% in much of the country, wages pitiable and a health system near collapse, there is plenty more for the populists to get their teeth into.

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Slovakia

Slo-where? Slo-what?

Jun 7th 2001 | BRATISLAVA
From The Economist print edition

Its people themselves are not quite sure of their own identity

AS THE poorer half of ex-Czechoslovakia, Slovakia has an identity problem. Few citizens of the European Union know anything about their prospective fellow member. George Bush once confused it with Slovenia. Ask Slovaks who is their most famous living compatriot, and you can hardly fault America's new president.

The question is easy for those who follow (North American) ice-hockey: Peter Bondra, of the Washington Capitals, for instance. But Martina Hingis (as in Hingisova)? A famous tennis-player, no doubt, but is she from Slovakia? She was born there, of a Slovak father. But her Czech mother whisked her off to Switzerland as a toddler. Or the late Andy Warhol (Warhola)? Artsy Slovaks love to go on about him, and his mother was indeed from Medzilaborce, a dreary town in eastern Slovakia. But she belonged to the Ruthenian minority.

Magda Vasaryova, a film star turned diplomat, is some Slovaks' choice. Cornered at a gallery opening in Bratislava, she patiently explains her country's plight. After all, it was a poor province of Austria-Hungary for 800 years, she says, whose best brains left for Vienna, Prague and Budapest.

"Dubcek," suggests a politician, recalling the Communist leader whose reformism in 1968 provoked the Soviet invasion—but that was of Czechoslovakia, before people made much of their Slovak identity. Besides, he's dead. "Paul Newman is half-Slovak," says someone. "That wrestler from Minnesota," the politician tries again, meaning Governor Jesse Ventura. "His parents are Slovak." At last another politician comes up with a real, live, notable Slovak: supermodel Adriana Sklenarikova (above). Very notable, in fact: "The longest legs in the world," beams Ivan Miklos, deputy prime minister of a country that has not yet exchanged Soviet slavery for that of political correctness.

A country? Yes, but of peasant stock, young (eight years old) and small (5m citizens), say some Slovaks defensively. Getting an identity takes time. More tellingly, many say it should never have become a country in the first place. "If Czechoslovakia hadn't split," laments one, "at least we'd have Vaclav Havel."

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Russia and its oligarchs

Who's next?

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From The Economist print edition

Vladimir Putin is flexing his muscles. But biffing is easier than building

UNTOUCHABILITY is not what it was. In the past few weeks three more rich and powerful men, all emblems of the chaotic and greedy years of Russia's recent history, have felt the cold breath of official displeasure.

The first was Rem Vyakhirev, the former boss of Gazprom, the grossly mismanaged national gas company, and probably the single most powerful businessman in the country. A single swift move from Mr Putin last week, and the company board booted him out and put in a Putin trusty.

Just as remarkable, if less conclusive, was the questioning by prosecutors a few days earlier of Roman Abramovich, a tycoon and a former top courtier of ex-President Boris Yeltsin. The authorities are interested in theft and fraud at Sibneft, an oil company he controls.

The third, lesser, victim is Andrei Vavilov, a former deputy finance minister who used to handle negotiations over Russia's external debt. He is now accused of embezzlement. All three men have strongly denied any wrongdoing.

The stamp of Kremlin involvement is plain. Where the rich and powerful are concerned, Russia's legal system is a political weapon, not a dispenser of justice. Likewise, state shareholdings in companies like Gazprom are mainly for politics, not profits. The demise of the latest three big guns follows Mr Putin's whacking of two other troublesome tycoons: Vladimir Gusinsky, a media baron, and the most manipulative of the lot, Boris Berezovsky. Both are now abroad (see table). In February, the Kremlin also forced the resignation of Yevgeny Nazdratenko, governor of the notoriously ill-run Maritime Territory in Russia's far east.

Ten men with money

	Job	Where?	Prospects
Roman Abramovich	Oil and aluminium tycoon, pal of Voloshin	Moscow	Fraud charges
Nikolai Aksyonenko	Railways chief	Moscow	Good, for now
Boris Berezovsky	Tycoon, politician, courtier	France	Financing opposition parties and television from abroad
Pavel Borodin	Former Kremlin property manager, now head of Russia-Belarus Union	Moscow	Legal problems in Switzerland, none at home
Anatoly Chubais	Former reformer, electricity chief	Moscow	Good
Vladimir Gusinsky	Media entrepreneur	Spain	Fighting extradition, bankruptcy
Yevgeny Nazdratenko	Former regional boss, now fisheries chief	Moscow	More chips
Andrei Vavilov	Former debt negotiator	Moscow	Embezzlement charges
Alexander Voloshin	Chief of Kremlin bureaucracy since Yeltsin	Moscow	Indispensable?
Rem Vyakhirev	Former boss of Gazprom	Moscow	Directorship (non-executive)

Source: *The Economist*

The simplest reason for all this is good housekeeping. Mr Putin prizes efficiency, respectability, discipline—words rarely associated with any of the six victims or indeed with the country's disorderly past.

Two big questions remain unanswered, though. Why these three now, and what about all the others? For all his faults as a manager, Mr Vyakhirev co-operated when the Kremlin needed to bankrupt Mr

Gusinsky's media empire; Gazprom obliged by suddenly calling in its previously forgotten debts. Mr Abramovich has been a model of adaptability, taking over the governorship of Chukotka, a destitute far-eastern province, supposedly to show the new caring face of Russian capitalism. Mr Vavilov had long been out of the public eye.

Second, business elsewhere still runs much as usual. The country's electricity monopoly, headed by Anatoly Chubais, has fought off attempts to make it more open and investor-friendly. The central bank, and the national savings bank it controls, are still scandalously badly run and unaccountable. Mr Nazdratenko has a nice new job running Russia's lucrative and mismanaged fisheries. The railways minister, Nikolai Aksyonenko, is creating an opaque intermediary company under the unconvincing guise of reform. There is still much murk at the top in industries such as aluminium, arms and telecoms. And the Kremlin's own property empire itself still seems to be run very much on the lines of the past.

One theory is that it is mainly a question of time. Even if Mr Putin had replacements to hand, he cannot remove all the barons at once. Loyalty to the people who put him in power has stayed his hand against some of their chums, like Mr Abramovich. Still an intelligence officer at heart, he may just like to keep his foes guessing.

All that would be grounds for optimism, at least in the long run. The state is certainly stronger than it was. But it is not better run. The evidence so far points to control, rather than reform, as the Kremlin's top priority. Mr Putin has yet to prove that he is willing or able to change fundamentally the system that created the people he is now so impressively biffing.

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The second term

Tony's big ambitions

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From The Economist print edition

If Tony Blair is to achieve his ambitions for the second term, he will have to make choices—and enemies

Get article background

THIS time it really is "historic". No previous Labour prime minister has been re-elected with a majority big enough to carry him through a full second term. From the moment of his 1997 victory, Mr Blair was haunted by this history of failure and determined not to repeat it. This made him cautious; and the caution made him puzzling. He has admitted that the first phase of New Labour was designed to reassure voters that Labour would not again make its old mistakes: trade unions could expect no special favours; there would be no old-style tax and spend; business would be welcomed as a partner. The precious second term allows him at last to show his true colours. But what are they?

To some, Mr Blair is Bill Clinton minus the complications (and minus the charisma, too). But David Marquand, a former Labour MP and now an Oxford don, draws a parallel with Margaret Thatcher. Like Lady Thatcher, Mr Blair's political genius lies in having reached across familiar ideological boundaries to the core constituency of his opponents. Both have a rootless quality. She was cut off by sex and he is cut off by upbringing from the cultures of their respective parties. Mr Blair calls this a strength: he is proud not to fit into the conventional political categories. It may also be his weakness: according to Mr Marquand, Mr Blair differs from Lady Thatcher in that he has not yet found a distinctive ideology of his own.

The things he did

You do not need an ideology in order to be busy. After 18 years out of office, Labour burst back in 1997 like a cork popping from a champagne bottle. Mr Blair freed the Bank of England and rewrote much of the British constitution. He half-repaired relations with the European Union by signing the "social chapter", promoting a more independent European defence policy and promising—pending a referendum—to join the euro. He pushed Britain to the forefront of NATO's Kosovo war and negotiated a half-peace in Northern Ireland. He launched a "New Deal" for the young unemployed and imposed a minimum wage.

He also made mistakes—and showed a rare ability to recover from them. The Millennium Dome became a symbol of incompetence. A protest against fuel taxes brought Britain to a standstill. Mr Blair was forced—twice—to sack his friend Peter Mandelson from the cabinet. But none of this damaged the government for long. On balance, and especially given Gordon Brown's successful management of the economy, it was a successful first term.

On balance, it was a successful first term. This doesn't make it a reliable pointer to the second

This does not make it a reliable pointer to the second. Now that he has reassured Britain, Mr Blair wants to transform it, not just run it competently the way it is. This puts him squarely in the Labour tradition—except for one complication. Winning power entailed creating New Labour, which in turn meant throwing away the tools—state ownership and planning, crude redistribution—that previous Labour prime ministers relied on. What can he do without them?

Through the cloud of speeches, three ambitions stand out. Mr Blair wants to change Britain's position in the world, to "modernise" its politics and to re-engineer the welfare state. With a renewed mandate, plus

all the political capital he hoarded during the first term, he can be forgiven for fancying his chances. But he might still fail.

Britain in the world

Mr Blair is no “declinist”. He believes that Britain can lead in Europe, not just take its place as a loyal member of the Union. Nor does he accept that leading in Europe implies weakening Britain’s bond with America. He argues that Britain has a “pivotal” role in world politics by virtue of its seat on the Security Council, closeness to the United States, membership of the European Union and the G7, the credibility of its armed forces and the power of the English language. Mr Blair has relished cutting a dash on the world scene as an evangelist for his “third way”, saviour of Kosovo and the first western leader to befriend Russia’s President Putin.

The second term could bring this world-bestriding statesman down to earth with a bump. In some foreign eyes, traffic jams, stalled trains and pyres of burning cows have turned Cool Britannia back into the sick man of Europe. Mr Blair is not going to be able to re-create with George Bush, his ideological opposite, the affinity he had with Bill Clinton. Gerhard Schröder, the German chancellor who seemed for a while to defer to the more experienced British prime minister, shows declining interest in Britain’s third way. Lionel Jospin was never a fan. When Mr Blair told the French parliament that “what matters is what works”, the French prime minister was unimpressed. A market economy was all very well, he said later, but not the “market society” which French Socialists suspect Mr Blair of trying to foist on Europe.

Traffic jams, stalled trains and pyres of burning cows have turned Cool Britannia back into the sick man of Europe

Besides, to change Britain’s position in the world, Mr Blair has to change Britain’s attitude to Europe. This a harder job than it may sound in the immediate afterglow of re-election. He says that he wants to resolve British ambivalence towards the mainland “once and for all”, but the opposite has happened on his watch so far. Since 1997, the British have become more suspicious of the EU, not less. More than seven out of ten oppose joining the euro, almost half favour leaving the EU itself and most of those who would like to stay would also like to trim the EU’s powers.

This is a fragile base from which to win the euro referendum he has promised to call when the five economic tests for entry laid down by Mr Brown have been met. Mr Blair promises to pronounce on these tests within two years, which gives him precious little time to turn opinion in favour of the euro even if he could be confident that developments on the mainland would buttress his arguments for joining. The chances are that they will not.

Lady Thatcher said in Bruges 13 years ago that she had not rolled back the frontiers of the state in Britain only in order to see them re-imposed from Brussels by a European super-state. Mr Blair offers two answers to this. First, he dismisses as “theology” the possibility of the EU becoming a super-state. At last December’s Nice summit, Mr Blair infuriated some of his European partners by blocking some of their steps towards “ever closer union”. Second, he claims that Britain is winning the economic argument inside Europe. His prize exhibit here is the Lisbon summit of March 2000, after which he boasted that the EU had moved decisively from the mainland’s “old social model” towards a less regulated and more open economy.

Mr Blair dismisses as “theology” the possibility of the EU becoming a super-state

Really? The “theology” of the super-state still has believers on the mainland. The German chancellor and foreign minister are more (in the case of Joschka Fischer, the foreign minister) or less (in the case of Mr Schröder) frank advocates of turning the EU into something akin to such a state. Mr Jospin talked a fortnight ago about the need for a European “economic government”. As for winning Europe’s economic argument, this claim is premature. After Lisbon, a summit this year in Stockholm was a flop. Plenty of mainland politicians continue to say that the EU’s job is, precisely, to protect Europe’s social model from the cold winds of globalisation.

Mr Blair claims that Britain has no need to choose between America and Europe. The closer Britain is to each, he says, the greater its value to both. But here, too, the matter is not quite settled. During the Kosovo war Britain was a bridge, if a wobbly one, between the two halves of the Atlantic alliance. It may be harder in the second term for Mr Blair to bridge the gap between the EU and an American administration with uncongenial views on climate change, missile defence, China and the Middle East. Mr Blair insists that the EU’s defence initiative poses no threat to the primacy of NATO. Some in the French

government hope it will do just that.

A new politics

“Are you a pluralist or a control freak?”, Paddy Ashdown, the former leader of the Liberal Democrats, asked Mr Blair. The answer is still pending. Mr Blair protests that no control freak would have complicated his own life by devolving power to new parliaments and assemblies in Scotland, Wales, Northern Ireland and London. But far from proving that Mr Blair is a pluralist at heart, his reforms have persuaded many people of the opposite. The disappointed constitutional reformers of Charter 88, a pressure group that was thrilled by Labour’s election in 1997, ran an advertising campaign during this one depicting the prime minister as a Pinocchio, with a fibber’s nose to match.

His first-term constitutional reforms were not conceived with pluralism in mind

It is possible that Mr Blair is genuine when he says that one of his ambitions is to “reconnect” people with politics. But he does not appear to see constitutional change as the instrument. His first-term reforms, inherited in the main from John Smith, the former party leader, were not conceived with pluralism in mind. Scottish devolution was a way to head off the Scottish Nationalists’ demand for independence, and the Welsh assembly was offered because Wales would otherwise have resented Scotland’s Parliament. The Northern Ireland Assembly was part of an attempt to end the province’s civil war—a virtuous aim in itself but not evidence of a general preference for spreading power from the centre.

If Mr Blair had really believed in that, he would not have tried in both Wales and London to override local preferences by putting his own lieutenants in charge of the new power centres; nor neutered his own government’s Freedom of Information Act; nor ruled out, as Labour’s manifesto seems to, turning the House of Lords into an all-elected chamber. He could have pushed devolution further in England, and called the referendum on voting reform which he promised both to Mr Ashdown and to the voters of 1997. But on the eve of this week’s poll he mused about the disproportionate power proportional representation tends to give small parties. In retrospect, the lofty talk of using voting reform to herald a “progressive” realignment in British politics seems to have been so much flannel intended to keep the third party sweet in case he needed it.

Will Mr Blair use the second term to make amends? Further reform of the Lords, devolution in England and another look at proportional representation make cautious appearances in Labour’s manifesto. If, as some argue, Mr Blair is the true heir of Gladstone, valuing diversity for its own sake, he will seize these opportunities to weaken the power of the over-mighty centre. But as Vernon Bogdanor, a professor of government at Oxford University, points out, this would mark a break with Labour’s past. A party intent on engineering equal social outcomes, across regions as well as classes, is bound to think that doing so requires a centralised state. Mr Blair is no socialist, and not much of an egalitarian either (he believes in “equal worth”, not equality). But he is no less keen than his Labour predecessors were on using the state to engineer desired outcomes. This is the idea at the heart of his third way.

A new welfare state

Mr Blair talks of imposing a third post-war “settlement” on Britain, one that will combine and transcend Attlee’s creation of the welfare state after 1945 and Lady Thatcher’s pro-market reforms after 1979. The linking of opposites is to be achieved by the third way, the main idea of which is to make the state cleverer and more entrepreneurial, helping citizens to help themselves rather than spooning out “bog-standard” (as Mr Blair’s spokesman called comprehensive schools) services through unimaginative bureaucracies.

Mr Blair resents nothing more than being labelled a softer sort of Tory

This vision does not entail shrinking the state, as Thatcherism tried to. Mr Blair resents nothing more than being labelled a softer sort of Tory. He continues to believe in the power of government to make the lives of people better, even to make them better people. He sees the need for a “post-Thatcherite revitalisation and renewal of collective provision”. Whereas Lady Thatcher deliberately lowered citizens’ expectations of what the state could do for them, Mr Blair spent his first term—and this election—raising expectations.

He will not be able to meet them just by spending more on public services, though there will be a lot more cash for a while. Having built up big surpluses for its first two years, the government is to increase

spending over the next three years by almost 4% a year, with rises of 6% for health and education, and 11% for transport. But the relief will be temporary. Since this is faster than the growth rate of the economy, it cannot go on indefinitely without raising taxes. The Institute for Fiscal Studies reckons that Mr Blair would need to increase taxation by £5 billion ($7 billion) a year if he wanted to extend his spending spree beyond three years.

Mr Blair's hope is that the extra money will strip public-service providers of their excuse to resist his big reforms. Labour promises in the second term to "hit the ground running". Immediate ideas include streamlining the machinery of government, for example by bringing employment and social security under one roof in a new ministry of work and the family, and creating a "policy-delivery unit" in Downing Street.

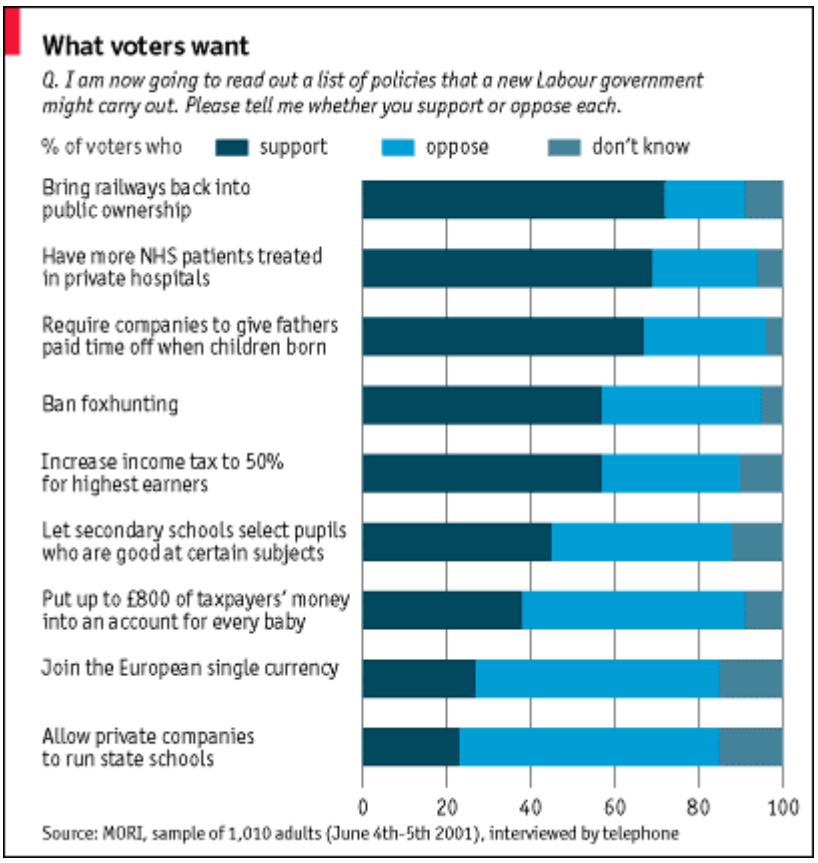
Tinkering with the machinery of government will be easier than finding a formula to rejuvenate Britain's public services. So far, the nearest thing to a big idea is a proposal to make greater use of the private sector and sweep away outdated demarcations. What does it matter, asks Mr Blair, whether a particular hospital is private, so long as the service is free at the point of use? But public-service unions from Unison to the British Medical Association have already voiced dismay at what they call this "back-door privatisation". Polls suggest that wider opinion is hostile to running public services at a profit. If this is his big idea for the second term, Mr Blair will have to overcome widespread prejudices as well as vested interests.

That would be a fight worth having, if the prize were indeed the transformation of public services. But Mr Blair's thinking on this is still a study in vagueness. There is no great merit in using private money to finance public services: quite often, this merely raises the cost to taxpayers with no offsetting benefit, apart from hiding that long-term consequence for a decade or two if the money is borrowed. Nor is there much point in Mr Blair turning to private providers if he will not embrace the heresy that users of public services have a better understanding of their requirements than Whitehall does. If he grasped this, Mr Blair would introduce real competition into public services so that schools and hospitals could fight it out for publicly funded clients, with the government concentrating on ensuring that everyone, regardless of income, has the means to get better services and make his preferences count.

Time to make choices, and enemies

Behind Mr Blair's blokeish manner is a compulsive competitor. His tennis partners say that he cannot bear to lose. But he also hates confrontation. He showed in Kosovo that he can be daring, but his watchword is caution. He would sooner bring a convert inside his big tent than make an unnecessary enemy. His biographer, John Rentoul, says he likes to string people along and keep options open, while waiting to see what falls into his lap.

The second term will provide fewer opportunities for prevarication and more for making enemies. A MORI poll this week for *The Economist* (see chart) suggests that he will face pressure to do things he has ruled out (such as renationalising the railways and increasing income-tax rates) and opposition to the things he wants to do (joining the euro, letting private companies run state schools, increasing school selection).



What of his three big ambitions? If Mr Blair's destiny is to settle Britain in Europe "once and for all", he cannot use Mr Brown's five tests to keep his euro-options open indefinitely, even if closing them means conflict with his chancellor. If he is really to modernise British politics, the pluralist in him will have to drive out the control freak, even if this makes his other aims harder to achieve. If he is to transform the public services, he will have to be bolder about competition, even if this means war with the unions. The danger otherwise is of stepping on to the familiar treadmill of higher spending and taxes, followed by disappointed expectations, followed by higher spending and taxes.

Like Lady Thatcher, Mr Blair does not want for self-belief: this is what they admire in one another. She had her "wets"; he is hemmed in by the Labour movement's own forces of conservatism. The difference is that she was fortified by a clear ideology which everybody in her administration could understand, and which gave them a sense of direction. If Mr Blair has an ideology, it is to run with the hare and hunt with the hounds. Only he knows exactly which way he is heading.

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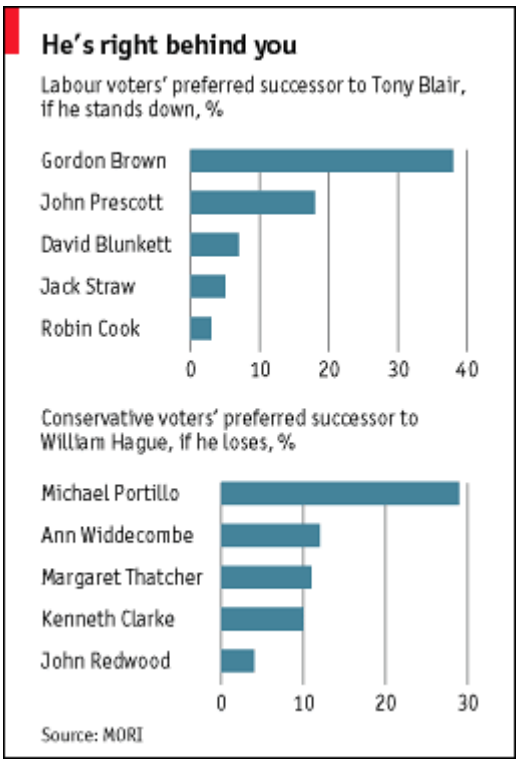
Leadership poll

The handbags are out

Jun 7th 2001
From The Economist print edition

Who, if anyone, should succeed Tony Blair and William Hague?

BLESSED, apparently, are the kingmakers. According to a poll conducted by MORI for *The Economist*, patience, like prudence, could prove a rewarding virtue for Gordon Brown: 30% of voters, and 38% of Labour supporters, would like the chancellor to succeed Tony Blair, should the prime minister step down during this parliament. If the public has its way, though, Mr Brown could be stuck with patience for a while: 67% think Mr Blair should serve a full parliamentary term, which Mr Blair has said he intends to do.



But gravitas, of which Mr Brown has bucketloads, is evidently not the only quality that impresses the electorate. His closest rival in the estimations of both the general public and Labour supporters is John Prescott, the pugilistic deputy prime minister. Despite—or perhaps because of—the short fuse and left jab he exhibited in the campaign's most interesting confrontation, 18% of Labour voters happily envisage Mr Prescott in Number 10. David Blunkett, also touted recently as a possible candidate (see article), is a distant third.

Just before the election, when our poll was conducted, William Hague's leadership seemed less than commanding: 55% of voters (and 40% of Tory supporters) thought a defeated Mr Hague should step down. The Tories have struggled of late to agree internally on a leader who is also palatable to the electorate. Our poll suggests an obvious remedy to this problem: Michael Portillo, the most popular successor among both groups.

The old problem of discordant tastes re-emerges, though, further down the Tory wish list. Lady Thatcher's interventions during the campaign provoked glee in the Labour Party and bad jokes about "The Mummy Returns". Yet 11% of Tory voters (against 7% of the total) would like her to bring the Conservative Party to heel once again. And while 15% of all voters would like Ken Clarke, the cuddly, Europhile ex-chancellor, to succeed William Hague, only 10% of Tory supporters concur.

For most of the rest of them, the problem is obscurity. Bill Emmott, this newspaper's editor, was included mischievously in the list of possible successors, and got more votes from Conservative supporters than did David Davis, the chairman of the public accounts committee, who is regarded by many as a serious candidate. (All right, Bill got one vote, and Mr Davis got none.) Perhaps Mr Davis should punch a few voters.

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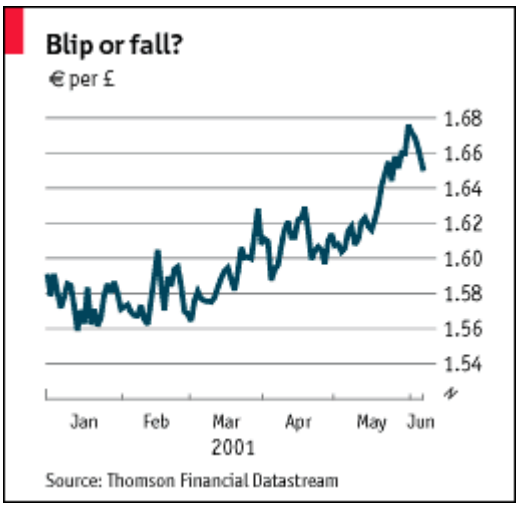
The pound and the euro

Maybe, say the money men

Jun 7th 2001
From The Economist print edition

The markets are reassessing Tony Blair's chances of taking Britain into the euro

FOUR years ago, Labour flunked early entry into the euro. Despite winning a huge majority in the 1997 election, the government imposed five tests for membership of the single currency. Ostensibly these were to determine the economic case for joining the euro. In reality, they were designed to close off the issue for the lifetime of the parliament.



This time, many believe it will be different. The prime minister is keen for Britain to join the euro. If he wants to accomplish this, he is likely to move fast to build upon his election victory. There is no reason why the Treasury, custodian of the five tests, should not deliver its verdict within a few months. Few doubt that they will be passed if that is what Mr Blair and Gordon Brown, the chancellor of the exchequer, desire. A referendum could then be called as early as autumn 2002. A yes vote would pave the way for Britain to enter monetary union in 2004, with euro notes and coin circulating a few months later.

As the election campaign drew to a close, developments in the currency markets suggested that dealers were beginning to attach some credibility to this scenario. Sterling dropped against the euro and hit a 15-year low against the dollar. Traders know that the pound will have to fall substantially against the euro if Britain is to make a success of joining it. At the least, it will have to fall by 10%, and some calculations suggest a devaluation of 20% will be necessary. So they are starting to anticipate such a decline.

But there is a long way to go. Before this week's speculation about early entry into the euro, the currency markets were placing only a 10% probability on EMU entry by 2004, rising to 25% by 2006, according to calculations by Deutsche Bank. This rating of the likelihood of eventual entry into the euro is much lower than three years ago. "The market has been putting a very low probability on an early referendum and an even lower probability on winning it," says Avinash Persaud of State Street, an investment bank. Even after the pound's decline on June 6th, it remained higher against the euro than when the election was called.

Formidable road blocks lie ahead for Mr Blair. For one thing, he must win the agreement of Mr Brown. The chancellor has made no secret of his unhappiness with the current institutional arrangements of the European Central Bank, which he regards as greatly inferior to those for the Bank of England.

Most important, public opinion remains hostile towards Britain joining the single currency. Although a majority of people think that eventual membership of the euro is inevitable, an early referendum will still be risky. The Danish government lost its referendum to join the euro last September even though it started with a lead among voters and commanded general support from business and the media. Mr Blair cannot expect such backing: business is divided and much of the press is viscerally hostile. The political costs of losing a referendum would be high. The prime minister would lose much of the authority gained in the election.

Much will hinge on what happens to the euro itself. While it remains chronically weak, it is hardly a glowing advertisement for membership. Despite this week's jitters on the currency markets, the pound is not out for the count yet.

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Bagehot

The ascent of David Blunkett

Jun 7th 2001
From The Economist print edition

Tony Blair is back, amid fresh speculation about who will eventually succeed him

IT IS not definite enough to be a rumour. Perhaps you could call it a sentiment. Whatever the right word, the fact is that at some point in the past few months the name David Blunkett and the phrase "future prime minister" have for the first time begun to crop up in the same paragraph of Britain's political conversation. This is peculiar. For a start, the job is not vacant: Tony Blair made it plainer than ever during the election that he intended to serve a full second term. And if Mr Blair does have an heir apparent, it is surely his next-door neighbour, the brooding, brilliant Gordon Brown. It is widely reported, and it may even be true, that Mr Brown made Mr Blair promise him the succession at the dinner in Islington at which he agreed to give his friend a clear run at the Labour leadership after John Smith's death. Since then, Mr Brown has fulfilled his part of the putative bargain. As chancellor of the exchequer he has given Labour an invaluable reputation for economic competence. He organised the campaign that has just landed the unprecedented second term. How did that interloper Blunkett butt into the narrative?

The first part of the answer is that if politics is a game of momentum, Mr Blunkett has it and Mr Brown does not. Mr Brown's second-best job in life is the one he has right now, at the centre of things at the Treasury. He will go nowhere voluntarily, unless it is to Number 10. Mr Blunkett, by contrast, is upwardly mobile. For several months the prime minister has been telling whoever would listen that Mr Blunkett had done a "brilliant" job as education secretary—and education, remember, is Mr Blair's thrice-hallowed priority in government. Word that Mr Blunkett would receive his just reward by becoming home secretary in place of Jack Straw was one of the few pre-reshuffle rumours that everybody believed.

Such a move, marking Mr Blunkett's ascent from the engine room of Blairdom to the bridge itself, was enough on its own to start the gossips going. But news that Mr Blunkett intends to publish a book in the autumn summing up his political philosophy has added to the intrigue. He is being helped by Tom Bentley, his former researcher and now head of Demos, Mr Blair's favourite think-tank. As it happens, Mr Brown is rumoured to be writing such a book too. Why would busy men at the very top of the government bother if they did not see these books as rival manifestos in a future leadership contest? Reporters who ask Mr Blunkett straight get the usual brush-off: there is no vacancy for prime minister. He sometimes adds a less usual one: that he cannot foresee Britain accepting the idea of a blind prime minister in the near future. Funny, that. When Margaret Thatcher was education secretary, she said that Britain was probably not ready for a female prime minister.

Whatever people think of his politics, Mr Blunkett is universally admired for his personal odyssey. Born almost completely blind, at the age of four he was taken from home in a bus and deposited in a special boarding school on the far side of Sheffield, where the boys in his dormitory cried themselves to sleep at night. He was still a child when his father died a slow and painful death, after falling into a vat of boiling water at a gasworks. A headstone was beyond the family's means so he was buried in an unmarked grave. All the misery of those years made the young Blunkett "very angry". At 16, he says, he began to see that history was a struggle between those with power and wealth and those who had neither. This was 1963, when Harold Wilson's talk about using the white heat of technology to create a better world inspired a new optimism. His college offered to train him as a piano tuner, a lathe operator or a Braille shorthand typist. He chose the Braille—but he also joined the Labour Party. By 22 he was the (youngest ever) member of Sheffield council, which he was to go on to lead.

Too good to come true?

Education secretary, home secretary—and prime minister hereafter? To complete the fairytale, Mr Blunkett would need to surmount formidable obstacles. Unable to read the papers in his red boxes, Mr Blunkett has had to spend long hours as education secretary listening to tapes, and his workload will probably have to rise at the Home Office. The premiership might stretch even his stamina too far, though

he has a legendary facility for storing an encyclopaedia of facts and arguments in his head.

Mr Blunkett's boosters call him the outstanding success of the first term, a minister who really managed to "deliver": higher standards in primary schools, for example, and performance-related pay for teachers. They praise a supple intellect that has let him evolve as a politician without being gulled by the latest fad. As a municipal socialist when Thatcherism was rampant, he came to understand the limitations of the old left. This made him a genuine Blairite, but a plain-speaking, practical one, less given than his master to abstract rhetorical flourishes. Though not much favoured yet as a future leader—a MORI poll for *The Economist* has him running a poor third behind Mr Brown and John Prescott—much could change when he is home secretary.

All in all, a lovely story—though naturally, since the leadership is at issue, another version is doing the rounds. In this one, Mr Blunkett's record at education is said to have been mixed: the few ideas that worked were inherited from the Conservatives, and the rest were forced on him from Downing Street. His childhood miseries have made him hard, incapable of accepting poverty as an excuse for failure. The supple political intellect admired by his supporters boils down to a social authoritarianism that will make him an even less liberal home secretary than Mr Straw. Some unkind souls go so far as to suggest that Mr Blunkett's chief virtue is not being Mr Brown, whose brilliance is acknowledged but whose succession is feared. The second term may turn out to be more intriguing than expected.

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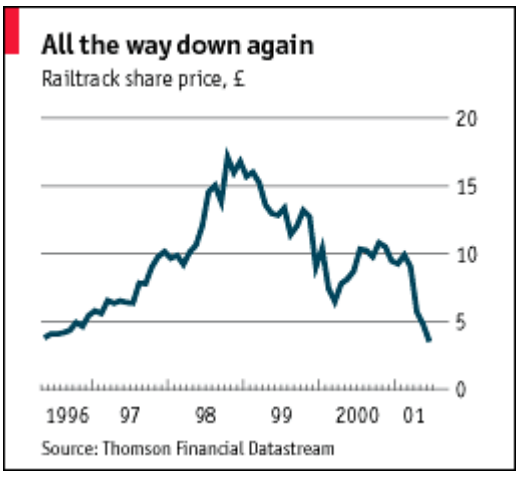
Railtrack

Mess on the rails, continued

Jun 7th 2001
From The Economist print edition

Railtrack's share-price collapse brings a restructuring of the industry closer

IN ITS ten-year transport plan, the government forecasts that up to half the £60 billion needed to finance the modernisation of the railways will come from private investment. That figure has always seemed optimistic; but this week's collapse of Railtrack's share price makes it look unrealistic. After ABN Amro, an investment bank, said it thought the shares were worth no more than 58p, their price fell to £3.50. At their peak in November 1998, they were worth £17.68. At this rate, Railtrack is not going to be raising much capital in the financial markets.



What to do about Railtrack will be one of the first tasks for whoever is unlucky enough to get the transport job in the next government. Pretty much everybody now agrees that the model of rail privatisation imposed on the industry by the Conservatives does not work. However, the government has no appetite for renationalisation, despite the urging of the railway unions—and the public, of whom, according to a poll conducted by MORI for *The Economist*, 72% support renationalisation. So what are the alternatives?

One radical solution now being discussed is the possibility that Railtrack could be referred to the Competition Commission on the ground that it is a monopoly which is failing the public. The commission could recommend, for instance, that the company be broken up into smaller regional units.

This would fit in with proposals made by David Begg, chairman of the Commission for Integrated Transport, and Jon Shaw, a transport economist. They have recommended a fundamental restructuring of the railways. Five regional train-operating companies would be responsible for both train and track operations.

The Begg paper, now being discussed by government advisers, also calls for a review of the way the industry is regulated. The dual-regulation model in which the Rail Regulator and the Strategic Rail Authority (SRA) divide up responsibility for controlling the industry has led, the paper notes, to personal conflicts and blurred responsibilities. It says that Railtrack's adversarial relationship with the regulator, Tom Winsor, has contributed to its falling credit rating.

Mr Begg, who advises the government, is also arguing that the incentive structure that was put into place when the industry was privatised is flawed. More than 80% of Railtrack's revenues are fixed. That gives the company little incentive to invest in efficiency or growth. The SRA's performance targets have had a perverse effect, too. They have encouraged train operators to stretch journey times in their timetables to minimise the risk of trains arriving late. Some journeys now take longer than they did 100 years ago.

The train-operating companies are increasingly fed up with the dire state of the network and would welcome fundamental reform. Three of the biggest companies, First Group, Stagecoach and National Express, have already begun to talk to the SRA about the possibility of re-integrating the industry. The government will have to make a decision soon, because those companies' franchises are due to be renewed in the next few months, and they need to know what is going to happen to the industry.

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Foot-and-mouth and tourism

The policy of silly walks

Jun 7th 2001 | LINCOLN
From The Economist print edition

Reuters

Foot-and-mouth disease is not the only reason why most of England's footpaths are still closed

ASIDE from a recent upsurge of cases of foot-and-mouth disease (FMD) in Yorkshire, the plague is receding. The latest advice from the agriculture ministry is that in FMD-free counties, all footpaths should be open, and in infected areas, all except those within 3km (1.9 miles) of an infected area should be open.

Odd, then, that most footpaths are still closed. This week, according to the Countryside Agency, only 42% of paths are open. This includes urban footpaths, so in the countryside, the figure is probably about 10% lower.

If this persists into the summer tourist season, it will be a problem for rural businesses. The English Tourist Council (ETC) estimates that four out of five holidaymakers in England expect to go walking as part of the holiday that they take in the countryside. With so much of the countryside still cut off, it is not surprising that the ETC estimates that bookings of cottages, bed and breakfasts, caravans and the like are down by about 35%. Businesses that rely exclusively on walking and hiking are in trouble. The Youth Hostels Association estimates that it lost £5m between March and June because of FMD.

The government has called for more footpaths to be opened, as has everyone from the Ramblers' Association, the walkers' main lobby group, to the National Farmers' Union. According to the agriculture ministry, not a single case of FMD has been attributable to a walker during this outbreak. So why are so many footpaths still closed?

Central government has the power to order footpaths to be opened if it wishes; but it has chosen to leave this delicate matter in the hands of local government, and some councils are more open than others (see map). Conspiracy theorists suggest that in some areas FMD is being used as an excuse to restrict access to rights of way that landowners did not much want to open or maintain in the first place.

Although Devon was badly affected by FMD, it has been quick to reopen footpaths, probably because tourism is so important to its economy. Its county council has long been vigilant in the matter of maintaining footpaths and enforcing rights of way across private land. According to an Audit Commission report in 2000, 89% of footpaths in Devon were "easy to use". In Staffordshire, similarly, which scored 88% in the Audit Commission report, 90% of paths in its Peak District are now open.

The picture in Buckinghamshire, East Sussex and Lincolnshire is quite different. These are all FMD-free counties, but have kept

their footpaths closed for the longest. The entire network in Buckinghamshire was closed until last week; in East Sussex most footpaths open only this weekend. Lincolnshire, the fourth-largest county in England, still has only 6% of its footpaths open. The council in Lincoln argues that it has always “erred on the side of caution during the crisis”, even to the extent of out-cautioning MAFF. With little inland tourism, it can afford to do so.

Opponents of the policy argue that the draconian closure measures have less to do with FMD than with the council’s general attitude towards access and rights of way. The head of the Labour group, Robert Parker, argues that the county “does not have a commitment to keep the footpaths open at the best of times”. In the Audit Commission’s report, only 46% of Lincolnshire’s footpaths were classified as “easy to use”. It scored lower than any of the shire counties.

Lincolnshire, according to the ramblers, is one of the places where both the land and the council are controlled by people who have little enthusiasm for enforcing, or maintaining, legal rights of way. North Yorkshire, which scored only 64% in the Audit Commission’s report, is also fingered for its unsound attitude to the ordinary man’s right to ramble.

As the government has passed the buck to the counties, so Lincolnshire County Council has passed the buck on to parish councils. They have been asked to say whether they want to see their local footpaths reopened. Parish councils are even more influenced by the views of local landowners and less interested in the rights of urban ramblers than are higher levels of local government. Hardly surprising, then, that 43% have so far said no. To Mr Parker, this is not local democracy but an “abdication of responsibility”, as the parishes have received no scientific guidance on the subject from the council, let alone the latest MAFF guidelines.

Lincolnshire is hardly a tourist trap, but it has two of the best long-distance footpaths in England, the Macmillan Way and the Viking Way. In a recent survey by the council, 25% of businesses said the restrictions imposed as a result of FMD were hitting their business. Come the summer holidays, that will bite.

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Lord Archer's trial

A battle of diaries

Jun 7th 2001
From The Economist print edition

It is possible to have too many Economist diaries

FAT, red and glossy, *The Economist* desk diary is, we bashfully admit, a status symbol to which many aspire. Lord Archer, successful novelist, former deputy chairman of the Conservative Party who also hoped to be mayor of London, liked our diary so much that he bought two for the same year. This interesting fact is at the centre of Lord Archer's trial on seven charges of perjury and conspiracy to pervert the course of justice.

Reuters

Fancy a date?

The charges against Lord Archer, whose career has spanned politics, business and the theatre, stem from his successful action in 1987 against the *Daily Star*. The paper claimed that he had slept with a prostitute, Monica Coghlan. Lord Archer admitted that he had paid her £2,000, but won his case after he produced an alibi for the night in question. He was awarded £500,000 in damages, a record at the time.

That alibi is now being disputed, which is where the diaries come in. Lord Archer, described as "not a diary man", left the tiresome business of keeping tabs on his appointments to his then private secretary, Angela Peppiatt, the trial's blonde leading lady.

Mrs Peppiatt told a jury at the Central Criminal Court this week that she was asked by Lord Archer to buy a new *Economist* diary for 1986 and fill in a series of fake entries shortly before his libel action began in 1987. She said that Lord Archer had given her three of the entries on a piece of paper; others were taken from his genuine personal diary. She had complied with his order, though reluctantly, because she did not want to lose her job. But she was so worried about what she was doing that she wrote what she described as an "insurance policy", witnessed by a colleague, detailing precisely what had happened. She also kept photocopies of all the key documents. She then delivered the "fake" diary to Mishcon de Reya, a firm of solicitors which was acting for Lord Archer in the libel trial.

Asked if she had received a reward for doing all this, she said she had not, although Lord Archer's practice was to keep a "picnic basket" full of blank, signed cheques for his various personal and business accounts which she would then complete. But the defence, cross-examining Mrs Peppiatt, suggested that she had taken her children out to expensive restaurants and claimed the bills as expenses.

Lord Archer listened impassively, occasionally blowing out his cheeks and sighing. Alongside him in the dock, seated as far away as possible, was his former friend, Ted Francis, a television producer who is also charged with conspiracy to pervert the course of justice. It was his claim in the *News of the World* that Lord Archer had asked him to help construct an alibi for his libel trial that set off police inquiries. The trial is expected to continue for another month.

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Iran's presidential election

Khatami faces a treacherous second term

Jun 7th 2001 | TEHRAN
From The Economist print edition

Iran has seen big social changes, but where does it go now?

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One perfect rose

AN EXHIBITION on show as Iran prepared for its presidential election on June 8th told a salutary tale. Mikhail Gorbachev, the exhibition recalled, was a gullible reformist whose misguided attempts to improve a Communist government ended up destroying the Soviet Union. Another section of the exhibition described Muhammad Khatami's continuing efforts to reform Iran's Islamic regime. The exhibition was ordered by Ayatollah Ali Khamenei, Iran's supposedly impartial supreme leader, and a caption duly contended that "Khatami is not another Gorbachev". But the exhibition's title, "The Great Lesson", carried the message that a vote for the cautious Mr Khatami could be a vote to destroy the Islamic revolution.

That seems a wild exaggeration, given the mild pace of reform. But, by the time the votes have been counted this weekend, Mr Khatami will have strolled to a second presidential term. His victory is not an indication of overwhelming support. The president, a cleric, is a declared believer in Iran's version of Islamic government, but the more radical of his electoral supporters, looking towards western liberalism, are not. Iranians are aware, however, that Mr Khatami is the only reformer acceptable to Mr Khamenei and the powerful clerical establishment gathered behind him. At present, it makes no sense for radicals to rally round anyone else.

At first sight, Mr Khatami's first term can be judged largely a failure: his bid for political reform was spiked by the clerical establishment. Even so, the past four years have had two momentous effects.

First, Iranians have got used to speaking their minds, and this despite the warning that the country's hardline judges have banned pro-reform publications and jailed prominent reformists. With a little goading, many people now dare conduct the sort of political discussion that Mr Khatami himself would not countenance, and might well land them in jail.

Second, nearly everyone in Iranian politics, apart from a hardline fringe, now claims to favour some sort of reform. Take the nine candidates put up by the conservatives to try to dent Mr Khatami's majority. The presence of only one cleric among them shows that even conservatives recognise the waning of the clergy's prestige. And distinctly liberal ideas have been discernible in their campaign literature. The question is no longer whether Iran changes, but how, and into what.

None of this means that the conservatives will do the president's bidding, or help him to pursue his gentle policy of reform over the next four years; they hanker for control of that policy. Nor does it mean that hardline judges will abandon their efforts to imprison opponents. After arresting some 60 dissidents this spring, they recently summoned several of the president's close allies for informal "chats": a sure sign, it is thought, that further arrests are in the offing.

Mr Khatami has shed his naivety, but he may find his second term as frustrating as his first. One difference could be a rearrangement inside the reform movement. Until now, the movement has made room both for radicals, who say they expect Iran soon to be run by non-clerics, and the lukewarm, who think the present system needs only tinkering. It is generally agreed that this cohabitation cannot last.

In theory, disagreement and debate, within both the reformist and conservative camps, could edge Iran further towards the pluralistic future that Mr Khatami envisages. But there may be difficulties. Many people on both sides of the reform-conservative divide have scant regard for democratic principles.

Moreover, revolutionary Iran lacks the secure economic and social foundations it needs if the transition is to be smooth.

When Mr Khatami came to power in 1997, he inherited a debt-bound economy labouring under cronyism, corruption and mismanagement. A timely rise in oil prices, coupled with a sensible monetary policy, helped stave off crisis. But the president and his ministers have dragged their feet on reforming the centralised economy, partly because they could not agree what form the changes should take, and partly because they feared social unrest.

Iran is sitting on a time-bomb. During the 1980s, overshadowed by the eight-year war with Iraq, the population grew by 3.5% a year: the 18m Iranians born during that decade now account for over a quarter of the population. Some pundits reckon that the economy is generating no more than half the 1m or so jobs the growing-up war-babies will require each year for the next ten years. By 2005, when Mr Khatami steps down, unemployment could have risen to at least 5m.

The social costs of decades of mismanagement are all too apparent. Small-scale industrial unrest is endemic. Iranians are divorcing at a rate associated more with the degenerate West than a devout Muslim nation. At least 2m Iranians are drug addicts. And brains are draining away: according to a recent survey carried out at Tehran's Amir Kabir University, 80% of students in the capital want to emigrate.

So, as Mr Khatami enters his second term, optimism has to be severely diluted. He is, it is true, showing more interest in the economy than he did when he came to power, and he has become a more capable politician. But with the conservatives bent on keeping things as they are, and the radicals itching to turn them upside down, the popular re-elected president may again find himself caught in the middle.

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Israeli-Palestinian ceasefire

After the Tel Aviv suicide-bomb

Jun 7th 2001 | JERUSALEM
From The Economist print edition

Sharon and Arafat drew back from all-out war, but remain on the brink

"RESTRAINT is strength," proclaimed Ariel Sharon on June 3rd at a Tel Aviv hospital where dozens of teenagers lay injured after the suicide-bombing at a beach-front discotheque on June 1st. This is not a philosophy that Israel's prime minister has notably espoused during his long and turbulent career in the army and in politics. But the very enormity of the attack, which killed 20 young Israelis, may have provided the shock that Israel and the Palestinians needed to draw back from the brink of all-out war.

Mr Sharon's restraint was purchased, literally at the last minute, by a public statement from Yasser Arafat, on the morning of June 2nd. Under strong international pressure, and threatened with an invasion that would have endangered his regime, the Palestinian leader said that he would "do all that is needed to achieve an immediate, unconditional, real and effective ceasefire." He followed through with instructions to his police to implement his ceasefire decree "by force if necessary". Israeli aircraft and tanks, under cabinet orders to strike at the Palestinian Authority, were told to stand down.

At mid-week, despite sporadic incidents in the West Bank and Gaza, and despite the scepticism voiced by all, the ceasefire seemed to be holding. On June 6th Israel began slightly to relax the draconian blockade it had imposed on the territories after the bombing. Crucially, the Bush administration then sent George Tenet, the CIA chief, to talk about how the ceasefire is to be monitored, and how to reinstate the long-lapsed "security co-operation" between the two sides.

The fortunate presence in the region of Germany's foreign minister, Joschka Fischer, helped to stay Israel's fist, and to ease a ceasefire out of the Palestinians, at least until American diplomacy lumbered into action. Mr Fischer, who had heard the bomb blast from his Tel Aviv hotel, shuttled frantically between Mr Sharon and Mr Arafat. His tone and tenor with the Palestinians were markedly more rancorous than Mr Arafat is accustomed to hearing from European statesmen.

After Mr Arafat had made his promise, he sought approval from the leaders of his own Fatah movement and the other Palestinian factions, including Hamas and Islamic Jihad. He got, or so it seemed, a yes for a ceasefire, if only to avert further Israeli attacks on his regime (though a no to any talk of ending the *intifada*). The ceasefire would mean, say Fatah people, an end to all military attacks, suicide or otherwise, inside Israel proper, and no more shooting at soldiers or settlers from within Palestinian-controlled areas. But later in the week this commitment appeared to have begun to unravel. "There is no change in our previous policy," said Mahmoud Zahar, Hamas's spokesman in Gaza. "We will resist Israeli attacks everywhere and by all means. There is no ceasefire."

Packing them into prison

Even harder for Mr Arafat is Israel's insistence that the Palestinian Authority should rearrest the 100 or so Hamas and Islamic Jihad prisoners freed from PA jails during the past eight months of fighting. It is also insisting on the imprisonment of another 200 Palestinians, including members of Fatah and officers in the PA's own security forces, who Israel says have been responsible for killing Israelis, whether in Israel or the occupied territories.

There is broad Palestinian consensus that Mr Arafat cannot meet this demand, save perhaps for the arrest of those Palestinians specifically involved in the suicide-bombings. "How can Arafat arrest Hamas people for 'violence' when everybody knows that Fatah people led the 'violence'?" asks a Hamas leader in Gaza. "If he moves against Fatah, he will fall on his neck." Perhaps this—which is what Israel's right-wing has called for—is the intention.

Before the Tel Aviv blast, Mr Arafat had made any ceasefire conditional on Israel publicly embracing the

other recommendations made by the Mitchell commission last month, including a freeze on all settlement-building. After the bombing, he made the ceasefire unconditional (as demanded in the report). But, say Palestinians, the basic equation still holds: no ceasefire will be sustainable if Mr Arafat cannot offer some tangible political relief to his people.

Logic points to the ceasefire leading to the implementation of the Mitchell report's call for "the resumption of full and meaningful [peace] negotiations". But here the broad base of Israel's national-unity government—which gave the country the strength to do nothing after the suicide-bomb—begins to collapse. The hawks say they will topple Mr Sharon if he gives way over settlements; the doves threaten to bring him down if he does not negotiate "meaningfully". Mr Sharon rises above both by insisting that he will be there "for many years to come", apparently ready to implement the Mitchell plan on a comfortably gradual timetable. The Palestinians, with dreadful decades of Israeli gradualism behind them, see things differently.

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Nigerian tourism

Holidays for masochists

Jun 7th 2001 | LAGOS
From The Economist print edition

The governor of Lagos wants to develop tourism. Make the place habitable first

WHEN a journalist tried to sneak into Nigeria as a tourist because the military regime was refusing visas to the foreign press, the immigration officer did not believe him. “No one comes to Nigeria for tourism,” he snapped, refusing the visa. But last week some 30 black mayors from American cities came to Lagos for the Black Heritage Festival, a carnival parade followed by some traditional culture and a visit to Badagry, a former slave-exporting port. The governor of Lagos, Bola Tinubu, then appealed to the mayors for advice on how to attract African-American tourists to the country from which their forebears were once taken in chains.

EPA

Whipping tourists into line

The mayors may be willing to help, but creating a tourist industry is an uphill task. Nigeria’s greatest living novelist, Chinua Achebe, was scathing: “It is a measure of our self-delusion”, he wrote in his book “The Trouble with Nigeria”, “that we can talk about developing tourism...[Nigeria] is one of the most corrupt, insensitive, inefficient places under the sun...It is dirty, callous, noisy, dishonest and vulgar...Only a masochist with an exuberant taste for self-violence will pick Nigeria for a holiday.”

That was almost 20 years ago, but little has changed. Other West African countries from the Gambia to Ghana have developed strong tourist industries, but Nigeria’s prospects may have worsened. Its own bluff president, Olusegun Obasanjo, told an international conference recently that Lagos, Nigeria’s commercial centre, was so disturbing and violent that no sane person could choose to live in it.

Home to 120m people on the malarial west coast of Africa, Nigeria is best known for corruption, military regimes and outbursts of sickening violence. Crime is over-familiar: even the wash-basins in its run-down hotels have “Hotel property. Do not remove” painted on them.

But Nigeria is also home to the greatest range of languages, art and culture on the continent. It has given birth to some of Africa’s greatest writers and musicians, though years of debilitating military rule have stripped writing and music of their vibrancy. The country’s first culture minister was appointed two years ago, but the ministry produces few ideas about how to save, let alone promote, Nigeria’s heritage.

The ancient walled cities of Benin, in the south, and Kano, in the north, are in a pitiable state of decay. Not far from Lagos, an ancient wall and moat built 1,000 years ago around the Ijebu-Ode kingdom now rot unattended in a forest. Most of Nigeria’s best artefacts—those that were not carted off by British imperialists—have been sold since independence, often illegally, and shipped out of the country. What is now left in museums is a sorry reminder of just how much is missing.

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Central African Republic

An old coup hand

Jun 7th 2001 | BANGUI
From The Economist print edition

The aftermath of an attempted coup is bloody and divisive

ALTHOUGH the presidential guard successfully foiled a coup on May 28th, fighting continued this week in the Central African Republic's capital, Bangui, and the total death toll is likely to be far more than the official figure of 32.Thousands of people have fled their homes, and government troops have been executing both suspected rebels and civilians who defy the curfew. The deserted streets are strewn with decomposing bodies, and residents huddle in churches for safety.

President Ange-Félix Patassé has turned down the peace talks proposed by the French government, and seems determined to stamp out the rebellion. But, as yet, his troops have been unable to secure the capital, and rebels hold the radio stations. Amadou Toumani Touré, an ex-president of Mali who helped bring peace to the CAR after army mutinies in 1996, has been dispatched to the scene by Kofi Annan, the UN's secretary-general.

The coup appears to have been mounted by General André Kolingba, the country's military ruler between 1981 and 1993, when he lost an election to Mr Patassé. Many of the soldiers remained loyal to him, and there have been several mutinies. This week he admitted that he was involved in the attack on the presidential palace, but denied that it was an attempted coup. The government responded by stripping him of his medals, and demoting him to private. It put a bounty worth $38,000 on his head, dead or alive.

Mr Patassé does not have to rely entirely on the dubious loyalty of his own troops. His 500-strong presidential guard has been bolstered by two planeloads of Libyan troops and armoured vehicles. Until a few years ago, a single Libyan soldier in French-speaking Africa might have been enough to bring the French Foreign Legion in. During the 1996 mutiny, when the CAR still contained France's biggest base in Africa, the French came to Mr Patassé's rescue. But the base was closed in 1998, and the French have lost interest.

The president is now a firm ally of Colonel Muammar Qaddafi's. So far, the Libyans have been restricted to guarding the presidential palace and ministers' homes, but they have set up a new radio station called Peace and Liberty. Mr Patassé has also been helped by Chadian troops and by fighters from Jean-Pierre Bemba's rebel movement in Congo, which has bases across the Ubangi river. This aid, however, is not entirely one-sided: the Congolese are reported to be filling dugout canoes with sofas and other looted household goods and sailing them back home.

The trade unions brought the country to a standstill in January in a series of strikes. But the latest trouble came as a surprise, even though the government had failed to pay its civil servants and, more foolishly, its soldiers. The main cause seems to have been General Kolingba's simple desire to rule once more.

The violence has again divided the country along ethnic lines, pitting southerners (loyal to the general) against northerners (loyal to the president). The army has been traditionally dominated by southerners: a UN peacekeeping force, which came in after the 1996 mutiny, had begun to restructure it to include all the ethnic groups. But the peacekeepers left last year—perhaps too soon.

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Iran's mismanaged industries

The sad tale of a textile factory

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From The Economist print edition

Clerical politics and bad management

SHORTLY before Iran's 1979 Islamic revolution, the entrepreneurial and philanthropic Hamedanian brothers bequeathed the trusteeship of their conglomerate to the great and good of Isfahan. According to the 1,350 workers at the Bafnaz textile factory, one of its divisions, it was a rotten decision.

When import restrictions were lifted a few years ago, and foreign textiles flooded Iran, the new managers hatched plans to sell off the decaying factory's plum site, and use the money to build a new plant. A group of Iran's senior clerics argued that the conglomerate should be controlled directly by them. The courts disagreed.

In 1999, two years into Muhammad Khatami's reforms, politics intervened. Ayatollah Ali Khamenei, Iran's conservative-minded supreme leader, told Ayatollah Hossein Mazaheri, his ally in Isfahan, to take over the conglomerate, perhaps with an eye to using the profits to help religious seminarians. But Isfahan's governor, an ally of Mr Khatami's, held up the sale of Bafnaz's site. The new plant, says Abdullah Koupaiee, Hamedanian's managing director, cannot be completed without money from the sale.

Partly as a result of the delay, the group is making a loss. Bafnaz is in a woeful state. In the winter, the factory ran out of money to buy raw materials. The workers sit idle, intermittently drawing reduced pay from Mr Koupaiee, a social-security fund and a state-controlled union. In May they broke the law, and demonstrated outside the factory gates. Having once thrived, Bafnaz is now quasi-nationalised, picked over and dying. It would all matter less if Iran's industrial landscape were not littered with sad factories just like it.

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E-strategy brief: Merrill Lynch

A reluctant success

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From The Economist print edition

In our fourth e-strategy brief, we take a look at Merrill Lynch. No big Wall Street firm had more to lose from the Internet, and none has made better use of it

AMID the current layoffs and cutbacks on Wall Street, America's largest stockbroking firm can breathe a sigh of relief. Two years ago, Merrill Lynch was widely tipped to be the biggest casualty in the securities industry from the Internet's disruptive impact. But since then, the firm has not only prevailed over many newer competitors built around technology; it has also adopted some of their most useful attributes—something that several traditional rivals have failed, at great cost, to do.

To understand Merrill's achievement, it is worth recalling how the industry operated as recently as the mid-1990s. Large commissions from retail customers could be had by offering little more than a quote and a trade wrapped in a forceful sales pitch. Merrill Lynch was the king of the trade. Its earnest men in neat Main Street offices had made Americans feel comfortable entrusting their future to something as inherently unsettling, if potentially rewarding, as the stockmarket. The strength of this relationship allowed Merrill to sail through the end of fixed commissions in the mid-1970s, a change that crushed many firms with more sophisticated, cost-conscious institutional clients who knew enough to demand better terms.

It was only when the Internet made the securities markets (almost) as transparent for Main Street customers as they were for sophisticated professionals that Merrill finally had to confront the full impact of price competition. Dozens of websites emerged in the late 1990s offering free share quotes and cheap trades. Huge marketing campaigns yelled out the message. Inevitably, their point of comparison was Merrill Lynch.

The numbers looked bad. Small trades that cost $100 at Merrill were advertised for less than $30 on the Internet, a crushing difference that more than made up for the online brokers' poor execution. Between June and December 1998, Merrill's public image shifted abruptly. Its share price fell from $50 to $19, despite a roaring stockmarket that had prompted the entire country to be (as Merrill had urged through its advertising) "bullish on America".

Inside Merrill, demoralisation was widespread. When the market capitalisation of the leading discount-cum-Internet stockbroker, Charles Schwab, exceeded Merrill's on one of the last trading sessions of 1998, it was front-page news in the *New York Times*. In its own inimitable way, Wall Street had voted on the future of Wall Street. Merrill was not it.

Under siege

Rumours of the firm's pending acquisition (and even of its demise) began to circulate, a devastating blow for a firm whose main product relied on selling confidence. Merrill's leaders, monitoring net new money coming into the firm, saw it slow down, at the same time as the flow of money into online brokers was accelerating. But still they held back from introducing an electronic product, mainly because of the "channel conflict" between electronic distribution and the 17,000 retail brokers who constituted the core of Merrill's competitive effort.

This army generated billions of dollars in commissions. But that was only a fraction of their true worth.

As part of the biggest single distribution system for securities in America, they made Merrill a favoured participant in lucrative corporate and municipal underwritings. Merrill's brokers also sold tens of billions of dollars of proprietary mutual funds, which generated handsome management fees, and they sold funds managed by other companies. These companies often returned the favour by passing their trades (and the commissions on those trades) back through Merrill.

The firm also had genuine concerns about the Internet. In the summer of 1998, John "Launny" Steffens, then head of Merrill's stockbroking arm, famously commented that "Internet trading should be regarded as a serious threat to Americans' financial lives." Self-serving? Many saw it that way at the time. A similarly contrarian position was held by the investment managers in Merrill's fund-management arm. They doggedly refused to pay high prices for technology shares and so underperformed during the boom.

"Internet trading should be regarded as a serious threat to Americans' financial lives."

In retrospect, these reservations seem more justified. Merrill confronted two different issues that appeared to be one: the Internet as an investment, which in most cases turned out to be a disaster, and the Internet as a means of making an investment, which could be more of an opportunity. Responding to the first, Merrill belatedly and unwisely turned bullish on the Internet only just before the peak of the market. Shares of Internet companies were sold on the back of in-house research, which became decidedly upbeat after the hiring of Henry Blodget, an Internet super-bull. The mutual-fund division fed the mania by pushing out an Internet fund whose miserable record is now quietly being rubbed out of history.

Damaging as this was, it mattered less than the way that Merrill responded to the second challenge: to capture the benefits of the Internet as a cheaper method to buy and sell securities. In autumn 1998, the firm brought in Michael Packer, a former senior executive at Bankers Trust, as a technology consultant. His first task was to survey existing e-commerce initiatives. Surprisingly, more than 130 were quietly under way. Less surprisingly, they lacked cohesion within a company-wide e-strategy—for no such thing existed.

In October 1998, Merrill hired John McKinley from General Electric to be their new head of technology and surrounded him with a group of half a dozen senior managers, including a repentant Mr Steffens. The group's mission was to devise a technology-based strategy that did not wreck the company's brand. Retail stockbroking was the first priority, with a system to be fully in place by the end of 1999. In the event, the deadline was met with four hours to spare.

Merrill began by meeting its own customers. Every member of the new technology group flew to San Francisco, home of the headquarters of Charles Schwab, where they met a cross-section of existing clients. They soon discovered that even the most loyal had "sandbox" accounts which they used to play with at rival online firms, and that those accounts were growing. Similar interviews in Texas, designed to check whether clients in San Francisco were more sophisticated than the average, found that they were not. There was no digital divide among investors: all were sophisticated, and all were potential defectors. "A decision was made then never to give a customer a reason to leave," declares Mr McKinley.

Counter-attack

D.E. Shaw, an innovative investment company that had been badly hurt by losses on securities during the 1998 bond-market crash, had discreetly launched a highly regarded discount broker earlier in the year. In February 1999, Merrill acquired the entire operation, including the organisation's 40 original software designers, who immediately sat down to work on expanding the capacity of their site to handle millions of accounts and far more features.

Several blocks away from Merrill's New York headquarters in the World Financial Centre, the firm leased three open-plan floors. A conference room was created by placing masking tape on the floor; for decoration, the employees' children dipped their hands in paint and made prints on the walls. Senior executives were imported from all the relevant departments to join the new recruits, and work began on redesigning Merrill's vast business of providing information, trading and underwriting services to

institutional clients. Another group, in Princeton, New Jersey, focused on Merrill's $550 billion asset-management business.

It soon became clear that there were huge opportunities to use technology to enhance Merrill's operations. Its primary business was creating, distributing and using information, and it was drowning in the stuff. The Internet offered a way to bring order and speed where there had been chaos. In the London offices of the asset-management operations, for example, 5,000 research reports arrived on the doorstep every Monday morning. Merely opening the mail had become a big problem.

Merely opening the mail had become a big problem

Merrill's vast institutional business confronted similar issues, if only because the firm's own 200 analysts fed the glut. And Merrill had, over time, developed numerous different trading platforms and services that were delivered to clients through incompatible systems, undermining the company's ability to cross-sell.

In June 1999, Merrill unveiled the first components of a new retail product. Called Unlimited Advantage, it charged clients annual fees based on the value of the assets that they held in Merrill accounts, not on the volume of their transactions. This avoided direct comparisons with pure Internet brokers, which charged by the trade.

But the fee schedule was impenetrable and, worse still, it was linked to a new Internet-based trading product that did not yet exist. Heavy advertising seemed more like an apology to brokers for introducing such a product than an appeal for fresh business. Wall Street scoffed; Merrill's shares, which had earlier perked up a bit, fell back again.

Customers, though, were more impressed, perhaps because the absolute level of fees was lower; perhaps because the cleverest clients realised that they could now negotiate even lower rates; or perhaps because the fee structure, in the right brokers' hands, seemed fairer. The new system made no charge, for example, for holding shares that a client owned but could not sell, such as those in his own company.

By October 1999, the first version of the new online product was ready; by November, the second version. In early December, the new web-based product was released, on time. Better still, it was packed with research, provided constantly updated information on accounts, and was easy to use. For fee-based full-service customers, trading was free; for anyone else, the cost was $29.95 a trade, roughly matching Schwab's charges. Gomez Advisers, an influential web-evaluation company, named it a top site.

Account transfers to rival firms duly dried up. Between June and the end of the year, Merrill's market valuation increased by 25%, vastly outpacing the wider stockmarket. Internally, however, there was still a fear that traditional Merrill clients, who had resisted using other online services in the past, would now talk to their brokers and use Merrill's expensive research—but then take the $29.95 option to trade. This could have been a brutal form of cannibalisation, says Jaime Punishill, an analyst with Forrester Research. But it turned out to be a false alarm. People seemed ready to pay more for human service. Meanwhile, the Internet-centred sites that Goldman and J.P. Morgan had designed for affluent customers did badly.

By mid-2000, Merrill was launching more than 200 software products a month. Its vast array of institutional offerings have now been consolidated into a single portal, mlx.com. A company backed by Merrill, Multex.com, creates electronic sites that consolidate investment research for a number of Wall Street firms. There is no longer a reason to be deluged by mail. In Tokyo, London and Princeton, Merrill's sprawling investment-management operations now collaborate minute by minute through a common electronic platform.

Not every web-based offering has been a success. An Internet shopping service provided to account holders has already been dumped. But others have been surprisingly well received. To capitalise on its newly created Internet link with customers, Merrill has built a broadcasting studio. Every day it sends out two hours of online video featuring comments and interviews with its analysts. The response to this service has been huge.

Could Merrill have done as well by doing nothing? Mr Steffens's warnings about Internet trading seem less absurd than they did at the time. The cheapest trading outfits, which offered the most radical alternative to Merrill's business model, are closing shop. Yet enough people are keen on a broad, cheap,

web-based trading product for Merrill to feel confident enough to open up in other markets. Through a joint venture with Britain's HSBC, a bank that is often rumoured to be planning to take over Merrill, it has begun selling its product in Britain.

Merrill is now in a far better position to provide the kind of services that sophisticated clients have wanted all along. These include seamless trading across borders as well as being able to move painlessly through the process of investigating and then buying a share—which means that all research on a company should require no more than a single click. Another click should provide information on the supply and demand for every security that the company has issued, and the relative merits of each as an investment. A final click should bring about a trade on the best terms.

Merrill, whose share price has recovered to $66, can now do all of these. But the process requires some irritating re-keying of information and the entry of different passwords. Such a bottleneck is an opportunity for a technically innovative firm—which Merrill, belatedly, now claims to be.

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Corporate restructuring

Japan Inc on the treadmill

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From The Economist print edition

Japanese companies are finding new ways to boost their profitability—although too many are still avoiding what is really needed

LAST year, corporate Japan was cutting costs mainly by shifting production to cheaper locations overseas and by shaking up traditional networks of suppliers. Nissan, for example, severed its ties with suppliers that could not offer it lower prices. This year, companies have, belatedly, been switching their attention to ways of reorganising their entire operations.

Some are shedding unprofitable divisions or product lines so that they can focus on their "core" businesses. The most striking example is Sega, which ditched its loss-making Dreamcast games console earlier this year in order to concentrate on making software for rivals' consoles. But Sega is an exceptional case, says Garry Evans, a strategist at HSBC Securities. Few companies have done anything quite so radical. For the most part, they are closing peripheral, not flagship, divisions. Typical is Denso, a car-parts manufacturer and subsidiary of Toyota, which recently announced that it will stop making mobile phones by the end of the year.

Companies are also putting their profitable non-core divisions to one side by means of strategic carve-outs and partial mergers, says Shintaro Hori, North Asian managing director of Bain & Company, a consultancy. These allow them, for example, to pool R&D resources and to consolidate overlapping operations. Hitachi and Matsushita, which announced an alliance on May 23rd, will share their expertise in developing new digital appliances. Stodgier businesses are also linking up. Kawasaki Heavy Industries and Ishikawajima-Harima Heavy Industries are hoping to fend off competition from South Korean rivals by merging their shipbuilding arms.

Outsourcing of production is also proving popular. Consumer-electronics firms, led by Sony, are selling their plants to independent electronics-manufacturing service (EMS) companies and then buying the products made in their former factories. Sony sold two of its plants to Solectron, an American EMS firm, earlier this year, and NEC wants to hand over some of its high-tech and phone-equipment plants to EMS firms. Other companies are even outsourcing to competitors. Nissan Diesel, a lorry maker, recently announced that it will stop making diesel motors for its four-tonne trucks and outsource them to the market leader, Hino Motors.

Manufacturers are also trying to make their production processes more efficient by installing supply-chain management (SCM) systems. Sharp, a consumer-electronics company, set up an SCM system at its Osaka factory in 1999. Since then it has raised the rate at which it fulfils orders instantly from 77% to 88%, and it has cut its inventory by one-third. Hundreds of firms have followed suit. Hitachi, Shiseido, a cosmetics group, and Ito-Yokado, a supermarket chain, are among those now installing SCM systems. The market for SCM software in Japan doubled in size last year, according to the Yano Research Institute.

Although still in its infancy, electronic procurement is also starting to take off, with companies such as Canon and Fuji Xerox shifting their procurement to the Internet. Fuji Xerox, which now buys only 3% of its supplies online, reckons that number will jump to 80% once its new system is installed in July.

All of this suggests that corporate Japan has come a long way from the days when restructuring was merely about squeezing costs. But it still has a lot to do. In the first place, improvements in manufacturing have disguised the lack of basic restructuring in other, less competitive industries such as construction and retail. The sickly construction industry is still trying to get rid of the massive debts and dud property that it collected during the market's bubble years—not helped by its failure to kill its own lame ducks. Despite falling orders, the number of construction companies has increased by some 15%

over the past decade, and is now at a record high.

The retail industry is also suffering from overcapacity. Although retail sales have fallen steadily since the mid-1990s, the total floor space available has risen. The opening of new stores has rapidly outpaced the closure of old ones. New stores are, however, cheaper, since land prices have dropped and there are now more low-cost, part-time workers to man them.

Labour pains

For all the restructuring done so far, corporate Japan has yet to tackle its excess labour. Kathy Matsui, a strategist at Goldman Sachs, points out that labour's share of national income has gone up since the peak of Japan's economic bubble in 1989. Companies' attempts to reduce labour costs have been feeble. Those that have cut their workforce—such as Nissan and Isuzu, which last month said it would shed 9,700 workers over the next three years—often find it easier because they have big foreign shareholders. Renault owns 37% of Nissan and GM almost half of Isuzu. Japanese-owned companies, if they do anything, still stick to early retirement schemes and a freeze on new hires.

There are several reasons why they find it hard to prune staff. One is that redundancy packages are a hefty expense that many weaker companies simply cannot afford. Another is that in Japan's *keiretsu* system of cross-shareholdings, many shareholders are corporate buddies facing similar dilemmas. They are unwilling to push for painful cuts in case they get the same treatment. Banks too are large shareholders, and they fear that redundancy costs might force firms into the red, exacerbating the banks' bad-debt problems.

But companies will not be able to enjoy the fruits of restructuring until the banks stop propping up corporate cadavers. Many of Japan's over-populated industries are mature, and the stronger companies in them can expand only at the expense of the weaker ones. Although bankruptcies have been rising, they have not been rising fast enough to give these stronger firms space to breathe. Around 20,000 companies went bust last year. This number will have to go up, maybe even to 1m, according to Katsuyuki Kumagai, a manager at Teikoku Databank, a research institute, before corporate Japan is freed of its suffocating excess capacity.

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3G telecoms

Think thin and crispy

Jun 7th 2001
From The Economist print edition

How much can 3G operators reduce the cost of building their networks?

Get article background

FOR the European firms building “third-generation” (3G) mobile-phone networks, hobbled by huge debts and technical problems, there was at last some good news this week. On June 5th RegTP, Germany’s telecoms regulator, clarified the rules governing network-sharing, making it clear that 3G operators would be allowed to share parts of their network infrastructure. Operators hope to save as much as 40% of the cost of building their Germannetworks as a result of the decision.

Network-sharing is controversial because of its potential to restrict competition. Two operators that build a network together are likely to compete less vigorously against each other than they would against other operators. Another worry is that, by allowing sharing, regulators will, in effect, rewrite the terms of the 3G licences granted for billions of euros through a series of auctions last year. Changing the rules retrospectively would set a dangerous precedent.

Fortunately, RegTP’s ruling avoids both these pitfalls. Network operators will be allowed to share only certain bits of equipment, such as towers and antennae; some of these things are already shared on today’s 2G networks. Each operator will still have to build its own “backbone” network linking base stations together. And sharing is permitted only in such a way that, if one operator’s network malfunctions or is shut down, other operators are not affected.

Sharing towers and antennae might not seem to provide much scope for savings. But these physical items account for a big chunk of overall costs, and sharing them can lead to savings of 20-40%. Since blanketing Europe with 3G coverage is expected to cost around $100 billion, this is serious money.

The German decision occupies the pragmatic middle ground between the Dutch, who have banned sharing altogether, and the Swedes, who have allowed even closer co-operation. The German compromise may well be adopted in other countries, such as Britain and possibly Italy, where a decision on sharing is expected soon. As a result, equipment manufacturers, such as Nokia, are already making base-station kit that is explicitly designed for shared networks.

Meanwhile, 3G is under attack on another front. “The 3G Squeeze”, a recent report by Merrill Lynch, says that 3G is in danger of being squeezed between so-called 2.5G technologies (essentially, 2G networks upgraded to handle data, but slower than 3G networks) and wireless computer-networking technologies such as 802.11b, which links laptop computers to office networks at high speeds. John Roy, one of the report’s authors, points out that the high data rates promised by 3G operators are designed for video, which users are unlikely to want to watch on the move. Lower-speed 2.5G networks may, in other words, be good enough on their own.

Does this mean that 3G networks will be entirely unnecessary? No, because 2.5G networks need more radio bandwidth than older 2G ones, and the required additional bandwidth has already been earmarked and sold to 3G operators. Besides, most operators plan to offer 3G services in densely populated areas at first, and to give customers hybrid handsets that can switch to 2.5G elsewhere.

According to Michael Minzlaff of Analysys, a telecoms consultancy, operators will start with these “thin and crispy” 3G networks, and then upgrade their capacity later. This means that, if the demand for high-bandwidth services fails to materialise, the upgrades will be unnecessary, and the bill need not come to $100 billion after all. 3G operators are in a hole, but the hole may not be quite as deep as it looks.

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South American airlines

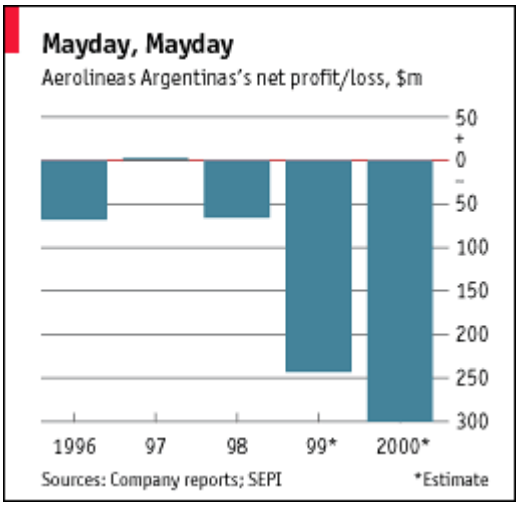
Don’t fly with me, Argentina

Jun 7th 2001 | BUENOS AIRES
From The Economist print edition

Argentina’s flag-carrier is struggling to stay airborne. So are many of its rivals

Reuters

WHEN aircraft were invented, people marvelled at how they seemed to defy the law of gravity. These days, it is remarkable how some of South America’s airlines defy the laws of economics, staying airborne despite apparently crippling debts. Aerolineas Argentinas has been performing the trick for years, burning up repeated capital injections and leaving behind a trail of red ink (see chart). But now the airline’s struggle to stay aloft may be close to an end.



Talks to try to rescue Aerolineas ended in deadlock late last month. These involved the governments of Spain (which owns 92% of the airline through SEPI, its state holding company) and Argentina (which owns 5%), as well as representatives of the staff (who hold 3%). SEPI says it will refuel Aerolineas with $350m of new capital only if all its seven unions sign new labour contracts involving pay cuts of up to 20%. Two unions are refusing. The crisis has caused a rift in the hitherto friendly relations between the two countries. On June 5th, Argentina demanded that SEPI (ie, Spain) try harder to seek a solution. But Spain’s prime minister, Jose Maria Aznar, signalled that his government was prepared to walk away, saying that it had already invested over $1.5 billion in an airline that was still not profitable.

In 1990, Spain’s then state-owned carrier, Iberia, led a consortium that bought control of Aerolineas from the Argentine government. But it could not make a go of the airline and last year, as it prepared for its own privatisation, Iberia transferred its Aerolineas shares to SEPI. Many Argentines blame Aerolineas’s plight on mismanagement by Iberia and SEPI. In turn, SEPI blames the unions for being unreasonable and the Argentine government for charging excessive airport taxes and breaking promises to protect Aerolineas from competition. But the main reason for failure, reckons Bob Booth of AvMan, an aviation consultancy in Miami, is that governments, especially distant ones, do not make good owners for airlines.

Aerolineas, which is losing about $30m a month, was flying less than half its scheduled routes this week. On June 6th, it scrapped more flights to preserve what little capital it has left. If SEPI does leave it to crash, would anyone else want to pick up the pieces? Maybe if some of the debts were written off, reckons Mr Booth. But who might buy it? The Argentine government is pinning its hopes on Eduardo Eurnekian, a local businessman who runs most of the country’s airports. Mr Eurnekian held talks with SEPI last month. But his plans are said to include keeping only half of the airline’s 6,700 staff. It is hard to see the unions accepting that.

Another possible buyer is TAM, which has just overtaken Varig as Brazil’s largest airline, and recently started flying from Sao Paulo to Buenos Aires, in competition with Aerolineas. But TAM’s owner, Rolim Amaro, says that, although he wants a big slice of the Argentine market, Aerolineas does not look a promising purchase.

Several North American carriers, including Delta and American, are looking to take strategic stakes in South American airlines. But they have plenty of willing, nay, desperate victims to choose from. Varig admitted this week that it was seeking an outside investor: its losses rose sharply in the first quarter, to 196m *reais* ($82m), and its debts, at $1.3 billion, are even bigger than Aerolineas's. Juan Posada, president of ACES, a Colombian airline, said last month that the region's aviation industry is suffering its worst-ever crisis: three-quarters of its airlines are losing money, he reckons, and a third are bankrupt.

The region's economic woes, the high dollar and rising fuel prices have all played a part in this. But poor management, excessive regulation and high taxation are also to blame. Sooner or later, some of the airlines now flying in the face of economic logic will come down to earth with a bump. This may be no bad thing. The stronger airlines should find it easier to take off once there are not so many lame ducks flapping around.

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Face value

Hard man Harry

Jun 7th 2001
From The Economist print edition

Harry Stonecipher is the tough outsider who is driving change at Boeing

WHEN Boeing took over McDonnell Douglas four years ago, it acquired a huge military-aerospace business and overtook Lockheed Martin as the world's biggest aerospace group. It also got Harry Stonecipher, McDonnell's boss, who became president and chief operating officer of the merged company. He is now vice-chairman—and he is staying on a year beyond normal retirement to complete the revolution that he inspired, symbolised most recently by the announcement that Boeing's head office is to move from Seattle to Chicago. Boeing wants to show that it offers more than jets and rockets, by expanding its new services businesses.

Mr Stonecipher's influence at this notoriously inbred company is plain. At the Paris Air Show later this month, Boeing's front man will not be its affable chairman and chief executive, Phil Condit, but Mr Stonecipher, an altogether different character. He is adept at schmoozing airline bosses and Pentagon colonels. But within Boeing he plays the hard cop to Mr Condit's soft cop. So it was when he first took over the day-to-day running of Boeing after the merger. What Mr Stonecipher saw horrified him. Boeing's civil-jet business was a mess. Ron Woodard, the ebullient salesman who ran the division, had started a price war to block the rise of Airbus, Boeing's European rival, in a booming market.

Boeing quickly got into difficulties, its factories choked with half-finished aircraft because suppliers could not keep up with production. In the autumn of 1997, the production lines had to be stopped so as to catch up. Airbus continued to advance, and the price-war policy proved a costly shambles. As the civil-jet division continued to struggle and Boeing's shares dived, Mr Stonecipher nudged Mr Condit to get rid of Mr Woodard, if only to signal a change. Mr Condit understood the case, and Mr Woodard duly left. The dismissal shattered Boeing's old executive culture, which had ensured that bosses were never fired, just shuffled.

Mr Stonecipher was also shocked by how little Boeing managers understood the bottom line. In a culture dominated by engineers, profit was seldom mentioned. Mr Stonecipher asked the company's finance director how he communicated with Wall Street. He said he did not. So Mr Stonecipher brought in Deborah Hopkins, a high-flyer from General Motors, as chief financial officer, with a brief to forge stronger links to the markets and to educate Boeing managers about profits.

One of the first to get the point was Alan Mulally, Mr Woodard's successor, who rapidly put the commercial-aircraft division back into profit. Mr Stonecipher claims some of the credit. "When I arrived, Alan was a great engineer and team leader," he says. "Now he is a fine businessman as well." Unsurprisingly, Mr Stonecipher was asked to stay on until next May because of his crucial role in helping Mr Condit transform Boeing into a services conglomerate.

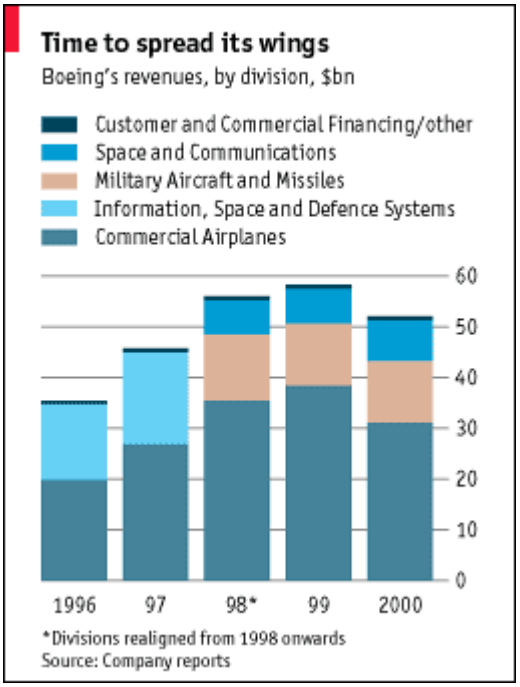
Until Airbus ate its lunch, Boeing was a proud American icon, the country's biggest exporter and leader in its field—but also a rather dozy place. A world where the European group had half the market looked bleak for Boeing's prospects, since aircraft sales are expanding by only 5% a year. With the immediate profit problems solved, it was time for wider horizons. "If you can't grow your revenues fast enough," says Mr Stonecipher, "you have to do something else."

This week brought two dramatic examples of what, for Boeing, that something will be. On June 4th, it won a $4 billion order from

the US Air Force, not for aircraft, but to upgrade the avionics on 500 veteran military transport aircraft. The model in question, the C-130, is actually made by Lockheed Martin. Boeing only moved into the aircraft-services business two years ago, seeing it as an area with big growth prospects.

Two days later, the company unveiled its blueprint for air-traffic management, which it hopes to develop with the Federal Aviation Administration as part of the agency's ten-year plan to overhaul America's creaking air-traffic control system. Boeing proposes using satellites to guide aircraft, with the ground controller reduced to a monitoring role. The company thinks this market could be worth $70 billion a year, some $20 billion more than the total market for jetliners.

There are other service markets towards which Mr Stonecipher is steering Boeing. One is broadband communications, offering passengers live television and high-speed data links. Boeing is hoping to announce its first customer in Paris, but there have been problems agreeing on how to share the revenues with the airlines. This week, Boeing also announced the opening in Dublin of the European head office of its financing company, Boeing Capital.



The Welch way

If this is all beginning to ring bells, it is not surprising. Before he became boss of McDonnell Douglas, Mr Stonecipher spent 27 years at General Electric, rising to become head of its aero-engine business in the mid-1980s. GE's boss, Jack Welch, famously revived the company's fortunes 20 years ago by bolting services on to the company's hardware.

Mr Stonecipher openly acknowledges the debt, and has even copied one of GE's ideas, the leadership centre for company executives. The centre he set up in McDonnell Douglas now serves the whole of Boeing; he and Mr Condit teach there once a month. That, not his part in the turnaround, is his biggest source of pride. Normally rather taciturn, Mr Stonecipher warms up when he talks about developing leaders. The hard man, it seems, really does care after all.

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Investment in Saudi Arabia

Old flames rekindled

Jun 7th 2001 | RIYADH
From The Economist print edition

The kingdom is once again becoming fertile territory for foreign companies

A QUARTER of a century ago, Saudi Arabia divorced the foreign firms that had helped to build its oil industry, gaining full custody of the world's richest oilfields. Now, squeezed by the cost of a growing population, the kingdom is welcoming some old partners back. Agreements signed on June 3rd will open three Ireland-sized chunks of virgin desert to international consortia, allowing them to tap and use whatever natural gas they find.

The deals are not only big, with investment costs expected to top $25 billion over ten years. They also put a giant foot through several doors at once. The upstream development of hydrocarbons had been a jealously guarded preserve of the nationalised monopoly, Saudi Aramco. The state firm will still control the Saudi oil reserves, a quarter of the world's total, including any that may be found in the new areas. But the international groups, two headed by ExxonMobil and one by Royal Dutch/Shell, will now take the lead in developing the kingdom's natural-gas reserves, which at an estimated 220 trillion cubic feet are thought to rank only behind those of Russia, Iran and Qatar.

Just as important, the agreements commit the foreigners to developing downstream uses over a 30-year period. In the most promising of the ventures, the South Ghawar field, won by a consortium of ExxonMobil, BP, Shell and Phillips Petroleum, plans call for building power, desalination and petrochemical plants.

Yet the gas initiative represents only the biggest, so far, of what may prove to be a bonanza of opportunities for private investors. Saudi officials put the price tag for upgrading basic services alone at $200 billion over the next decade. Demand for electricity, for instance, is expected to grow by 250% between now and 2020.

Perhaps more significant, unemployment, now 14% for male Saudis, is rising fast. The pressure will not let up soon, given a population (half of it under 18) that is growing at 3% a year. This surge in numbers, coupled with oil revenues that are restricted by OPEC quotas, has led to a slide in personal wealth. GDP per head, equal to America's 20 years ago, has slumped to a quarter of the American level.

These facts have forced the Saudi government away from state planning and towards active courtship of private capital. The momentum for change, stalled until the mid-1990s, is now accelerating fast. A slew of fresh legislation, including an investment law passed last year that allows 100% foreign ownership and tax breaks, is shaking up what had been a virtually closed economy. The government recently cut most import tariffs from 12% to 5%, and introduced a regulatory agency to oversee the telecoms sector.

The new attitude has already brought rewards. Foreign direct investment has doubled in the past year to reach $9 billion. Two projects, a $2.3 billion desalination plant built and operated by Japan's Sumitomo and a $3.4 billion contract to build and run 3,000 schools won by an American consortium, account for much of the jump. The gas deals will boost these gains—so much so that a local economist predicts they will add one percentage point a year to Saudi Arabia's GDP growth.

Yet the picture is not entirely rosy for outsiders. Uniquely among the Arab Gulf states, Saudi Arabia has so far been denied a seat at the WTO. The main sticking-point is internal trade, where Saudi distributors and retailers enjoy cosy market domination. The more serious, but vaguely defined, obstacle is simply the nature of the kingdom. The state makes up two-thirds of the economy, but its accounts are far from transparent. The application of laws can be patchy, inconsistent and brutal. Sooner or later, the pressure of Saudi need and foreign greed will change all this, too.

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OPEC

Is Baghdad bluffing?

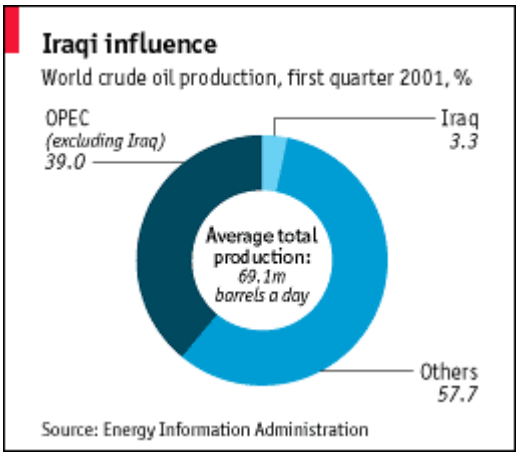
Jun 7th 2001
From The Economist print edition

OPEC needs to keep Iraq from destabilising the world's oil market

COULD Saddam Hussein really throw the world's oil markets into turmoil? That is the burning question among energy pundits, given the latest scare tactics deployed by the moustachioed marauder of Iraq. In response to yet another round of sanctions by the United Nations, he has cut off his country's oil exports again.

Taken at face value, this is serious. Oil markets are highly sensitive to supply disruptions, and Iraq is a big producer (see chart). If it really does withhold its exports of about 2.2m barrels a day for long, prices would skyrocket—and consumers would suffer.

Even OPEC would be hurt badly. That is why the ministers of the oil cartel, who met on June 5th in Vienna, said they stand ready to replace all the oil that Iraq takes off the market. Ali Naimi, Saudi Arabia's oil minister, made clear his readiness to tap his country's vast spare capacity (of 2.5m barrels a day) if it is needed to stabilise prices. The cartel took no immediate action, however; but it agreed to review the situation on July 3rd. That is because it has been messed around by Iraq before: it will act only if the export freeze proves to be more than the short-term bluffs of the past.



The reason for OPEC's curiously pro-consumer stance is that it knows Iraq could kill the goose that lays its golden eggs. A big supply disruption or prolonged high prices could plunge consuming economies into turmoil—and history has shown that oil shocks hurt oil producers as much as oil consumers.

What is more, the cartel is worried about a threat even bigger than Iraq's belligerence: global economic downturn. America's economy is struggling. Europe and Asia are in better shape, but the strong dollar (the currency in which oil is priced) has made their petroleum dearer, and so depressed consumption.

OPEC is also troubled by the sharp build-up in stocks in recent weeks—a dramatic reversal of the tightness of last year. Figures released this week, for example, showed unexpectedly strong increases in crude oil, gasoline and distillate supplies. That is good news for gas-guzzlers as America heads into its summer "driving season", but bad news for OPEC ministers trying to trump the latest card played by their wayward brother.

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Regulating the Internet

Tied up in knots

Jun 7th 2001
From The Economist print edition

Negotiators from 50 countries are meeting to formulate rules for governing cross-border lawsuits. These could have a profound effect on e-commerce

THE Internet's ability to span borders, destroy distance and unite the world's computer networks into a seamless whole looks wonderfully elegant to engineers, but awfully messy to lawyers. Previously cut-and-dried questions of legal jurisdiction—such as what country a particular transaction took place in—have now become horribly murky. Buy something in a shop, and you are clearly bound by the laws of the country where the shop is physically situated. But make a purchase from the same shop over the Internet from a foreign country, and it is not at all clear whose laws apply.

Untangling this legal Gordian knot is the unenviable goal of a treaty called the Hague Convention on Jurisdiction and Foreign Judgments. It is being discussed by delegates from 50 countries who met in The Hague on June 6th for two weeks of formal negotiations.

Much is at stake. The treaty covers commercial law, and it is intended to harmonise the rules for cross-border litigation between private parties. This includes disputes over patents, intellectual property, libel and defamation. Simply put, it would require the signatory countries to agree to enforce legal judgments handed down in other countries. This sounds fine in principle; indeed, a similar arrangement, the Brussels Convention, already covers EU countries.

The French ruling has in effect been imposed on citizens of other countries

But the Hague Convention would go much further, because it would cover a far larger number of countries, some of which have very different laws. Activists in the United States worry that, if the convention is agreed and ratified, American courts would end up having to enforce judgments against people whose actions were entirely legal under local laws. Such fears have been heightened by a French court's ruling last year that Yahoo!, a web portal, could not sell Nazi memorabilia through any of its international auction sites to users in France. Rather than attempt to filter its sites for users in different countries, Yahoo! banned such material from all its sites. The French ruling has thus, in effect, been imposed on citizens of other countries. The Hague Convention would formalise and grant international legitimacy to rulings of this kind.

For opponents of the convention, other nightmare scenarios abound. An American citizen could, for example, post something on the Internet and be sued for libel by somebody in another country where free speech is not protected. Or what if your invention or business model is stolen and patented by a rival in a foreign country with a lax patent regime? You could then be sued for patent violations in that country, and the judgments could be enforced against you at home.

To complicate matters further, different interest groups within each country would like the convention to be modified in different ways. Consumer groups want local laws to apply to consumers who buy things online, on the grounds that they cannot be expected to understand how laws might vary from place to place. But companies that wish to do business online do not want to get involved with myriad sets of regulations either. They would prefer to be able to impose "click-through" agreements on their websites, requiring customers to agree that transactions will be subject to the laws of the country in which the company is based.

It gets worse. In general, companies that export goods want their home laws to apply to the transactions; but so do firms that import goods. Clearly, you cannot have both. This means that, in some

cases, there is disagreement within single organisations about how the convention should be worded.

The danger is that the convention may undermine e-commerce. Companies might choose to block users in particular countries from accessing their sites, rather than be subject to those countries' laws, or decide against doing business online altogether. The implications for free speech are just as ominous. "The result could be that the Internet is reduced to the lowest common denominator, where websites avoid any but the safest content for fear of offending someone and being hauled into court," said Barbara Wellbery, a Washington lawyer and former e-commerce adviser to the Commerce Department, during a congressional hearing on the subject on May 22nd.

The result could be that the Internet is reduced to the lowest common denominator

Telecoms firms and Internet-access providers are concerned that, under some countries' laws, they would be liable for content travelling over their networks and so would have to start monitoring and filtering it. One suggestion, supported by telecoms firms, consumer groups and Internet activists, is that the section covering intellectual property should be excluded from the convention, so that the agreement applies only to disputes over the sale of goods and services.

This idea has been strongly opposed by publishers, record companies and other rights holders, however. They see the convention as a means of strengthening their ability to protect intellectual property in countries where it is currently difficult to make legal judgments stick—and are therefore about the only people with a kind word to say about the convention. It would, for example, make it easier to shut down websites containing pirated material, or to sue pirates in foreign countries for damages.

The negotiators meeting in The Hague face a near-impossible task in reconciling these different views. The idea is that final tweaks will be applied at another meeting early in 2002, at which point the treaty will be ready for ratification. But the previous attempt to finalise the convention's wording ended in 1999 without agreement, and the same thing may well happen again.

Part of the problem is that negotiation of the convention began in 1992, and the sudden explosion of the Internet in the mid-1990s undermined much of the work that had already been done. The convention was initiated by the Americans, who argued that, although their courts generally enforce the rulings of foreign courts, other countries do not always reciprocate. Ironically, it is now also in America, which has the most to lose from restrictions on e-commerce, that opposition to the convention is strongest.

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Sweden's Investor

Prepare to board

Jun 7th 2001
From The Economist print edition

Martin Ebner versus the Wallenbergs

IN HIS home country of Switzerland, Martin Ebner is feared and despised, but he is also grudgingly admired. Who could resist a man whose picture winks at viewers from his website? The pushy investor founded his BZ Group 16 years ago and began shaking up big Swiss companies by buying shares and then calling for better performance and changes to boards of directors. Even allowing for occasional failures, such as a recent rebuff by Roche, a family-controlled drug company, Mr Ebner has made Swiss business reconsider its more old-fashioned ways. Ask UBS and Credit Suisse, two banks that had to make big changes after he took an interest.

Reuters

Ebner deplores the lack of focus

But while Switzerland's business establishment knows Mr Ebner well, Sweden's is only just getting the measure of him. His latest foray pits him against the Wallenberg family, that country's most powerful industrial dynasty.

Although they no longer make things, the Wallenbergs still control Investor, a stockmarket-listed holding company worth some SKr108 billion ($9.9 billion). It holds large stakes in global giants such as ABB (engineering), AstraZeneca (drugs) and Ericsson (telecoms), as well as a bunch of smaller "new-economy" investments. Investor is run by Percy Barnevik, a renowned manager who joined in 1996 from ABB (where he remains non-executive chairman), and by Marcus Wallenberg, who became chief executive in 1999.

Last year, Mr Ebner spotted that shares in Investor were trading at a 30% discount to the group's theoretical net asset value. He started buying, first declaring a stake last December and then, last month, announcing that he had spent $800m to acquire 10.2% of Investor's voting rights. That makes BZ the second-biggest shareholder, behind the main foundation through which the Wallenbergs retain control.

Mr Ebner's simple point is that Investor will not be a true public company so long as it is controlled by the Wallenbergs. He has already suggested several ways to improve Investor's performance and narrow the discount on its shares from today's 23%, preferably to zero. First, it should buy back some of its shares. Then it should split new-economy investments into a separate company and spin this off. And it should improve its management of the remaining portfolio by narrowing its focus, thereby persuading capital markets to give it a higher valuation. Soon, if he follows past behaviour, Mr Ebner will be demanding a seat on Investor's board.

Investor is having none of it. This week it flatly rejected Mr Ebner's suggestions, saying it sees no need to buy back shares and fears that a break-up would destroy valuable "network" effects that result from its clutch of holdings. It pointed out that its shares have consistently outperformed the Swedish stockmarket.

The Wallenbergs are unlikely to see off Mr Ebner quickly, especially if they go on simply dismissing his claims. From an outside perspective, Mr Ebner has much to offer, not least because BZ and Investor have more in common than the latter might admit. Both are financial investors. Both claim to be active shareholders that want to work with management teams to get the best performance from their investments. Their mission statements are uncannily similar. Perhaps it is only opposites that attract each other after all.

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Agricultural trade

Patches of light

Jun 7th 2001
From The Economist print edition

Any progress in liberalising agricultural trade at the next round of global trade talks depends on the groundwork being done today

PROGRESS on agriculture is long overdue. Over the past half-century, global trade in farm products has been liberalised only slowly. While tariffs on manufactured goods have dropped from averages of 40% to 4%, agricultural tariffs have stayed in the 40-50% range. Over the same period, the volume of trade in manufactured goods has ballooned nearly 17 times, compared with less than six times for agriculture.

There is today, though, a growing enthusiasm for change. At this week's Asia-Pacific Economic Co-operation meeting in Shanghai, China inched closer to agreeing with its trading partners on a level of farm subsidies that would be compatible with membership of the World Trade Organisation (WTO), which it is seeking. In Washington and Brussels, agricultural reform looms large on the programmes of new legislation. And the WTO in Geneva has been tidying up the many loose ends left by the last (Uruguay) round of trade talks, completed in 1994, in preparation for what is expected to be an agriculture-heavy next round. The planning for those negotiations, to be launched in November, will begin in July.

The end of the Uruguay Round brought promises of enhanced market access for the crops of rich and poor countries alike. Tariffs were broadly frozen, and only liberalising changes were expected by the members of the soon-to-be-born WTO. But the reality has been one of unkept promises. Until recently, even the poorest countries still faced largely unchanged high tariffs and low quotas when trading with the world's economic powerhouses.

Japan is one of the most egregious offenders; for instance, its duties on most grains average about 63%, but a tariff on rice installed last winter was closer to 1,000%. Even when their tariffs have been reduced, rich countries have developed ever more complex non-tariff barriers (NTBs) and domestic farm subsidies in order to frustrate imports.

This has gradually eroded poor countries' trust in the global trading system and was at least partly responsible for the globally publicised collapse of the WTO's meeting in Seattle in 1999. Early last year, the WTO set out to restore some of the poor countries' lost trust by initiating a series of behind-the-scenes discussions to set the agricultural agenda for the new round of trade talks. Comprehensive proposals came, as expected, from such heavyweights as America and the European Union (EU). But they also came from up-and-coming economies such as Egypt, Poland, Turkey and, most recently, Nigeria. Delegates have stayed *in camera* into the night to discuss ideas from traders as small as Mauritius.

Delegates have stayed *in camera* into the night to discuss ideas from traders as small as Mauritius

The atmosphere at these meetings has been far more egalitarian than it ever was during the Uruguay Round. Now, having collected some 35 proposals from its members, the WTO is ready to begin drawing up a concrete draft agreement. Almost for the first time, the agricultural trade negotiations have real momentum—but will it be enough?

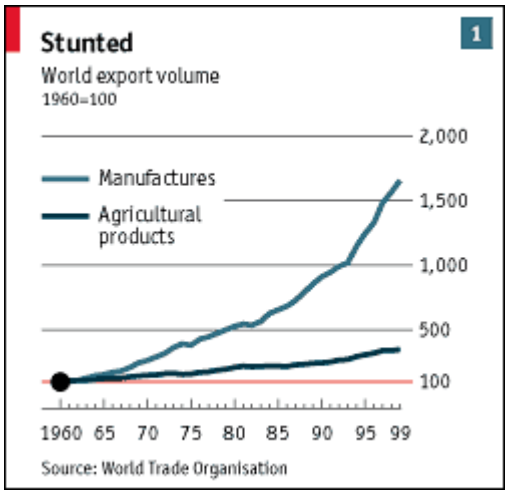
Distortion begins at home

Agricultural trade's most fundamental problems lie at the domestic level. Within the OECD, annual state payments to the agricultural sector exceed Africa's entire GDP. And domestic support in America, Europe

and Japan accounts for about 80% of the world's total.

The usual rationale for these payments is that agriculture provides social benefits not valued by the market: environmental protection, food security and the maintenance of rural communities, for example. The most important (and the least cited) factor, however, may be psychological. Japan's ambassador to the WTO, Koichi Haraguchi, says he realises that Japan's agriculture is less than efficient; other countries have natural advantages in production that could, if unrestrained by tariffs and domestic support, put Japan's farmers out of business. But the Japanese want to maintain their farms almost regardless. "Because they cherish their own agriculture, they are prepared to pay for it," says Mr Haraguchi.

The warm feeling gleaned by consumers from knowing that compatriots are out tilling the fields in the traditional way is an extra benefit of farming, like food security or a clean environment. But because the value of these benefits is not included in crop prices—so the theoretical argument goes—the industry must be subsidised. That line of reasoning has justified a slew of domestic support systems, with the most extensive and complex being in rich countries. It has also motivated a 64-page paper insisting on "the need to treat agriculture separately", submitted to the WTO and signed by virtually all West European countries plus Japan, South Korea and some other emerging economies.



In America, the justification for domestic support is less touchy-feely and more combative, less grass-roots and more corporate: the government must protect farmers against what Ann Veneman, the new agriculture secretary, calls "unfair and uncompetitive markets". Of course, consumers who pay to protect their farmers (be they American, European or Japanese) receive no protection from the higher food prices that result. In the EU, for example, the prices of lamb, butter and sugar are all more than twice the world market price.

Consumers who pay to protect their farmers get no protection from the higher food prices that result

Most farm support falls into one of two categories: price-related subsidies and direct payments to farmers. The former tend to be counter-cyclical, rising when market prices fall. That makes them distort markets even more, since domestic producers' competitiveness with the world's exporters is artificially enhanced. Direct payments, by contrast, do not change relative prices instantaneously. But they can still distort markets in the long term. Farmers who receive lump sums use some of the money to invest in capital, which enhances their productive capacity and pushes down the prices at which they can sell in the future.

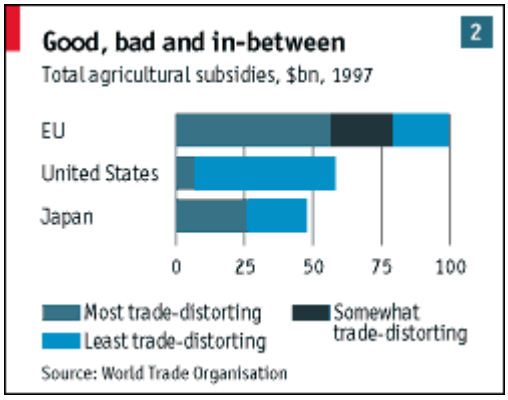
In the past five years, economic wisdom (and pressure from their trading partners) has persuaded rich countries to move from price-related subsidies to direct payments. America's 1996 farm bill and Europe's reform of the Common Agricultural Policy (CAP) have both taken steps in this direction.

Japan has chosen a different path: it now devotes most of its support to buying farmers' stockpiles of crops; its actual payments to farmers are falling. Before these changes were introduced, more than half of Europe's and Japan's support was considered trade-distorting (see chart 2), and reductions were required under the WTO's existing agreements.

But even as price-related subsidies and purchases of surplus crops have been cut, governments have found other ways to protect their farmers from the supposed ravages of global trade. For example, America's loan-rate guarantees, by which the government refunds the interest on farmers' loans when prices fall, clearly invite farmers to over-produce. And America's so-called "emergency" assistance, designed to shield farmers from unexpected market fluctuations, rose from $1.8 billion in 1998 to $7.6 billion in 2000.

Europe has also shown a willingness to rescue farmers from

adverse market conditions, something it does not do for any other industry. It has funnelled close to *euro*1 billion ($850m) to them in order to pay for the destruction of their herds brought about by the outbreaks of BSE ("mad-cow disease"). And now hundreds of millions more are going to finance the eradication of foot-and-mouth disease through the mass slaughter of livestock.



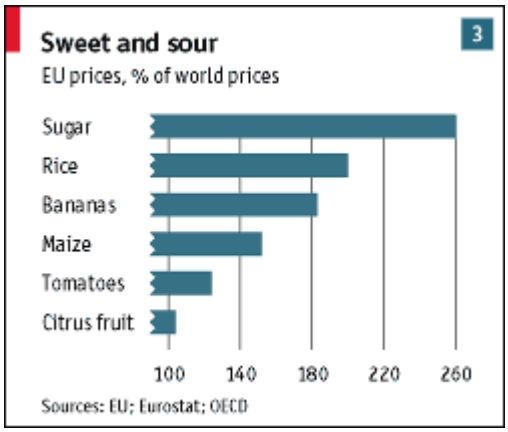
The funds needed for these payments were built into the budget of the agriculture directorate of the European Commission. In any other industry, companies would have to rely on insurance or credit to cover the costs of comparable external shocks to their business. The two epidemics threaten, however, to generate a backlash in favour of non-intensive and organic farming, with a consequent shift of CAP subsidies away from production and towards rural beautification.

Not all domestic support occurs in rich countries. In emerging economies, though, its rationale is generally different. India's recent proposal to the WTO recommends that any support aimed at alleviating poverty, rural development or the diversification of agricultural products be exempted from WTO-sponsored commitments to reduce domestic support. However, virtually any programme that gives money to farmers can be justified on these grounds. The same is true of Europe's claims for environmental protection and Japan's desire to prolong its agricultural tradition.

"The real pay-off from the Uruguay Round just hasn't happened"

Most developing countries' negotiating proposals ask for considerable concessions from their wealthier trading partners, with special treatment still reserved for their own support systems. Their case is strengthened by the fact that the market access they were promised after the Uruguay Round has not materialised. Even Joseph Glauber, the American agriculture department's deputy chief economist, readily acknowledges that "the real pay-off from the Uruguay Round just hasn't happened". In Europe, for example, some of the products that emerging economies are best equipped to export suffer the most distorted prices (see chart 3). If rich countries were to remove the subsidies that create these price differences, poor countries would benefit by more than three times the amount of all the overseas development assistance they receive each year.

Somewhere between domestic support, export policy and special treatment for poor countries lies food aid—the rich countries' habit of buying up crops when prices fall and then sending them to poor countries as aid. This is potentially the thorniest issue in the forthcoming negotiations. The EU's proposal on export competition calls food aid "a disgrace", its point being that poor countries need aid most when prices are high, not low. But from the standpoint of economic efficiency, their need must be balanced with the donors' ability to give. Countries can most afford to dispense such aid when prices are low, so it is hard to argue that their donations should be completely insensitive to prices.



Transparent tariffs

The WTO's members are still keen to keep domestic matters to themselves, so farm support enters the organisation's negotiating agenda only peripherally. Market access continues to dominate discussions, with emerging economies pushing for cuts in rich countries' protections.

While holding back the biggest plums of market access, rich countries have offered some concessions in the past few years. Their emphasis has been on "tariffication"—on replacing non-tariff barriers (such as anti-dumping measures, rules-of-origin restrictions, quotas and quality standards) with tariffs. Such efforts boost transparency as the volume of trade comes to depend more on the tariff rates than on hazy bureaucratic decisions. But switching from non-tariff barriers to tariffs can go only so far to promote agricultural trade.

Most countries agree that tariffs must fall further, and that the WTO must clarify its rules for tariff-rate quotas, which allow duties to rise after a certain volume of specific products has been imported. For example, the EU allowed 650,000 cubic metres of plywood to be imported tariff-free last year, on a first-

come, first-served basis. But because of the difference in seasons between northern and southern hemispheres, almost all the quota—which was filled by May—came from Brazil. American exporters, who came on stream later in the year, had to pay tariffs of up to 10%. They saw the quota as discriminatory, but had no WTO rules to help them.

Automatically triggered anti-dumping and "safeguard" measures in rich countries also distort imports. These trade regulations block imports, respectively, when world prices fall below a pre-set threshold and when imports exceed expectations. Even in its recent initiative to abolish tariffs on exports from the world's 48 poorest countries, Europe retained safeguards against floods of imported bananas, rice and sugar.

Likewise, America's extension of duty-free status to sub-Saharan African exporters, signed into law last May, allows the Commerce Department to step in if imports of clothing and textiles could cause "the threat of serious damage" to American competitors. The Cairns Group, an association of agriculture-exporting countries in the Americas and Oceania, wants to abolish such safeguard mechanisms entirely. But Europe and Japan insist on their continued existence.

Preferences are another sore point. The Association of South-East Asian Nations wants to ban programmes such as the EU's system favouring the African, Caribbean and Pacific group (ACP), basically a collection of its former colonies. An ACP-EU agreement signed in June 2000 includes an eight-year extension of preferences covered hitherto by a waiver from the WTO, but a renewal may not be forthcoming.

There is also a debate about the WTO's institutionalised system of preferences for developing countries, known as "special and differential treatment". Since the days of the WTO's predecessor, the General Agreement on Tariffs and Trade, rich countries have been required to give preference to imports that were deemed "of special interest to developing countries". Any new agriculture agreement, however, might switch the focus of these preferences away from specific products and towards specific countries instead.

But assigning preferences to countries comes with its own problems, according to David Roberts, the deputy head of the European Commission's agriculture directorate. South Korea has an advanced industrial sector but its agriculture looks like that of a developing country; Argentina is the exact opposite. Which of them should be called "developing" for the purposes of the WTO's system of preferences?

More immediate political concerns also threaten to block the road to a deal. For a start, the less than enthusiastic attitude of Japan is a cause for worry. Its delegation has been reluctant to define the details of an agreement whose scope and timeframe may be open-ended. In addition, the Japanese, who are the world's biggest net importers of farm products, believe that they will gain little in return for cutting tariffs on staples such as rice. They would rather tie agricultural concessions to progress in other sectors, in the context of a wider round of trade talks. South Korea takes a similar position.

The less than enthusiastic attitude of Japan is a cause for worry

Europe's comprehensive negotiating proposal includes two especially controversial points. First, it calls for import standards for meat products to be based on the treatment of animals in exporting countries. Many developing nations see this provision as protectionist, but non-governmental organisations' fierce promotion of the issue has persuaded a majority of EU member countries in favour. Compromisers want Europe merely to label well-bred sides of beef. Anything more might be an irresistible invitation to introduce politically popular protection.

Secondly, the EU has imposed some conditions on its willingness to negotiate. "We put everything on the table," says the Commission's Mr Roberts. But export subsidies, which now amount to about 9% of the agriculture directorate's budget of *euro*42.8 billion, may be a sticking point. Europe's spending on these subsidies has fallen from 55% of the value of exports in 1992 to 9.4% in 1998. All the same, they remain a contentious issue—so contentious that Maeve Doran-Schiratti, who deals with trade issues for Europe's agriculture commissioner, says negotiators would be better off without them. Nevertheless, Europe will only consider reducing the subsidies further if America, India and other big traders are ready to cut their export-credit guarantees (ECGs).

And that is unlikely to happen. In America's case, ECGs smooth the way for exports to developing countries; the government guarantees American bank finance for exports to markets where credit may

be hard to come by. Last year, over $5.4 billion of agricultural sales were underwritten in this way, roughly 10% of all America's farm exports. Terms for farmers' repayments of the loans are limited to three years in most cases, but $188m-worth had terms of up to ten years.

With that long to pay back the money owed, ECGs begin to look a lot like subsidies. America insists, however, that it is merely facilitating exports, and that ECGs should not count against its commitment to reduce export-related subsidies. So far the WTO has agreed with it .

There's something about a field

Poor countries' economies rely on agriculture; and rich countries, though fully industrialised, still cherish it. None of them wants to make substantial, unilateral cuts to their systems of protection. Concerns about hurting consumers by hampering trade have long taken a back seat to the wishes of the vocal domestic farm lobby. Mr Glauber's boss, Keith Collins, recalls the attitude of congressmen writing America's 1996 farm bill as, "We're not going to have this farm bill written in Geneva." But now, with more domestic support programmes potentially involved in international trade talks, reforms at the WTO and in its members' capitals will have to be more closely synchronised.

In the meantime, market factors can only intensify the pressure to reduce protection. Mr Glauber predicts that oversupplies in maize, rice, wheat and other crops, as well as increases in farm productivity, will persist for the next few years. That combination will lead prices lower, and consumers will doubtless want to reap some of the benefits—even in rich countries. Mr Haraguchi believes that productive agriculture and protected agriculture can continue to co-exist. But he also admits that pressure from world markets will force countries like Japan to make their own farms more efficient, which would be no bad thing.

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Bank regulation

Capital cushion fight

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Proposed capital charges for operational risk are exercising banks and their regulators alike

INTERNATIONAL banks, and their regulators, are wrangling over the level of additional capital that banks should be made to carry, as a cushion, against so-called "operational risk" that might damage a bank's health or even the financial system. Operational risk includes anything from computer failure and postal strikes to fraud and cock-ups of Baring-style proportions. Insurance companies, which you might think would steer well clear of this debate, have joined the fray, offering to replace bank capital with new-fangled insurance cover. They were in Washington this week trying to sell the idea to bank regulators from the Group of Ten countries.

Under present rules, banks carry capital against the credit and market risks that they run. Bold proposals by the Basel Committee of bank supervisors now seek to refine the charges for credit risk, as well as to add new charges for operational risk. The banks' responses to "Basel 2", which had to be in by May 31st, are almost all critical of the proposals for operational risk. Few agree even with the committee's definition of such risk: "the risk of direct or indirect loss resulting from inadequate or failed internal processes, people and systems, or from external events." Many dispute the inclusion of indirect loss, since it is so hard to quantify. Some say that "strategic" and "reputational" risks should be added. And that is just for starters, before even getting to the level of charges.

The committee has suggested that operational risk should account for roughly 20% of a bank's regulatory capital. Since it has also said that the overall capital charge should stay about the same, banks have been looking for a 20% reduction in charges for credit risk. In vain. Hong Kong complains that its banks will face a capital charge 2.5 percentage points higher if the Basel proposals are applied in their crudest form—with most of the increase being for operational risk.

Privately, regulators agree that the 20% figure is too high and will come down, but by less than the banks would like. The horse-trading can be followed on the Basel Committee's website, where many bank responses are posted.

The banks' biggest beef with the charge for operational risk is that the levels, by the most basic method, are set according to a bank's gross income. What kind of incentive is it that rewards banks for reducing their income? The proposal offers three further levels of sophistication in measuring operational risk, all of which the banks find either flawed or too complex. A "standardised approach" would rely on industry-wide loss data divided by business lines—such as corporate finance, trading or retail banking—providing a standard factor by which a bank's volume or gross income in that business would be multiplied to arrive at a capital charge. Then there is an "internal measurement" approach, using a bank's own loss data, multiplied by a formula for "expected loss" and by a factor for how the supervisor rates the bank's risk controls. Finally there is a "loss distribution" approach, which allows the bank to use its own probability analysis, although neither supervisors nor banks think the technique can be used yet.

The big problem is insufficient data. There are plenty on so-called "expected" losses, such as predictable levels of credit-card abuse, failed trades, even petty fraud. But the aim of the charge for operational risk is to cover the unexpected, such as a bomb blast or big losses by a rogue trader. How many events like that have there been over the past decade? How statistically relevant is a decade-old event?

All the same, data collection and data-pooling are going ahead. There are even some commercial databases on offer. One comes from NetRisk. It is based on data that Bankers Trust, an American bank now owned by Deutsche Bank, began to collect in 1993. That is being added to by the MORE consortium,

a joint effort by a dozen big banks, and by PricewaterhouseCoopers, an accounting firm. The other offering comes from a subsidiary of Zurich Insurance, called Zurich IC Squared, which offers a ten-year database online. The source of its early data is, once again, Bankers Trust. Supervisors find themselves using the same data too.

Banks worry that some operational risk will be double-counted as credit or market events—for example, bad documentation that leads to credit failure. There is also a debate about where to put reputation risk, since a blow to reputation can sink a bank. The regulators exclude reputation risk, says an insurer, because it happens slowly, and a bank can be unwound or sold—as in the case of NatWest, a British bank sold to Royal Bank of Scotland.

The debate on this and other topics could run for years; the banks, certainly, want more time for consultation. Yet deadlines loom. A framework for Basel 2 and its equivalent in the European Union, a draft capital-adequacy directive, is meant to be ready by the end of the year, in order to be implemented in 2004. Banks and supervisors will need at least that time to prepare themselves, once they know what to prepare for.

A debate with the insurance industry has only just got serious. Insurers do not normally lobby together, but two lobby groups, BAIWG and PCIIWG (do not ask what they stand for) are presenting bank regulators with ideas for lightening the capital charge that banks must bear for operational risk. Big chunks of banks' operational risk, such as professional liability and computer fraud, are already insured. Regulators agree that this already merits some offset against a capital charge. If insurers can concoct insurance cover for a wider range of risks, then the capital offset would be bigger.

For that to happen, regulators want to be satisfied that there would be immediate payouts (not a hallmark of insurers), and that there would be legal certainty, with no weasel clauses to let insurers off the hook. Insurers must be satisfied that they will not be left as a lender of last resort in a systemic crisis. At the discussions in Washington, the very definition of operational risk was still a sticking-point.

On the fringes, but maybe destined some time to take centre stage, are ideas to let the market impose discipline on the banks, at least as far as operational risk is concerned. Catastrophe bonds linked to earthquake and storm risk have been sold to investors, and so has contingent capital, in the form of callable equity. Adriana Cronin of Blanch Crawley Warren, an insurance-broking firm, would like to see an "opbond", based on a portfolio of operational risk covering the combined risks for a number of banks. Rating agencies would be needed to analyse and rate the portfolio backing the bond.

Most insurers think a capital-markets solution for operational risk is a distant goal. The nearer one is to bring their centuries of actuarial skills to bear to help banks save capital, and so to tap a rich new market of, potentially, 30,000 banks.

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Rating agencies

Reluctant watchdogs

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Shunning a regulatory role

RATING agencies ought, by rights, to be thrilled that their services may be needed to set bank-capital requirements worldwide. Yet the two biggest firms, Standard & Poor's (S&P) and Moody's, are alarmed by proposals by the Basel Committee to use their credit ratings to set how much capital banks must put aside for each loan.

Ratings embodied in regulation might be seen to be influenced by regulators, says S&P's president, Leo O'Neill. "The franchise would be lost. It would be self-defeating." The move, says Moody's in a note to the Basel Committee, "could erode rating-agency objectivity." And that could debase what the agencies see as their greatest asset, that is, "reputation capital".

Rating agencies are hardly strangers to conflicts of interest. For decades, they have received most of their fees from the companies they rate. They even have a creeping regulatory role already. In America, for example, the Securities and Exchange Commission (SEC) requires that the bulk of the trillions of dollars stuffed into money-market funds, savings vehicles not guaranteed by the government, carry top or near top ratings from at least two of three SEC-approved agencies (Moody's, S&P and Fitch).

These issues were raised again at a conference on June 1st at New York University's Stern School of Business. A paper by Richard Sylla (entitled "A Historical Primer on the Business of Credit Rating") summarised the most recent research and suggested that, although the rating agencies are far from perfect, over long periods they have acquitted themselves pretty well. Default rates rise as bond ratings decline. That is an indication that agencies have a pretty good idea which securities are vulnerable.

With most of the banks under threat from a ratings-based capital charge, the agencies would prefer to see charges based on the internal ratings of the banks themselves. But for less sophisticated banks and markets, that is not yet an option. External ratings will be wanted in parts where the big agencies do not reach.

In its own submission, S&P says that the Basel Committee should caution against using rating agencies in a way that could influence their rating methods. Inconsistent rating regimes could encourage "rate-shopping" by borrowers and lenders, Moody's says.

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Banking in Utah

From Mormon to mammon

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Utah is fast becoming a financial centre, thanks to a convenient loophole

"THERE is more to Salt Lake City than Mormons," says Mayor Rocky Anderson. He hopes that next year's Winter Olympics will demonstrate this to outsiders, especially if his efforts to make it easier to buy alcohol in the city succeed. More appropriate than sozzled tourists, in the home of that hugely wealthy institution, the Church of Jesus Christ of the Latter-day Saints, is Utah's rapid emergence as a financial centre. It is an emergence, moreover, that bothers the Federal Reserve and its chairman, Alan Greenspan.

Utah is home to a curious sort of financial institution known as an "industrial loan corporation" (ILC). Such corporations have been around since the 1920s, when they provided the sort of low-quality, high interest-rate industrial loans that ordinary banks shunned. In 1986, following some embarrassing and costly failures, ILCs were required to be insured with the Federal Deposit Insurance Commission (FDIC). In 1987 the ILCs survived congressional legislation designed to shut down "non-bank banks", thanks to a loophole introduced by an opportunistic senator from Utah. Since then, they have flourished, as a way for non-banking companies to own a bank insured by the FDIC and regulated by neither the Federal Reserve nor the Office of the Comptroller of the Currency. This is something that America's other banking laws have expressly sought to prevent.

Assets under management in Utah have risen from $2.9 billion at the end of 1995 to $59 billion in September 2000, and to $82 billion in March. This has prompted regulators in California to reform its legislation so that "thrift and loan" companies there can compete for the business.

However, according to Lou Callister, a lawyer in Salt Lake City, the quantity of red tape in California means that Utah remains a friendlier place to do business. There are few restrictions on the banking activities of an ILC—unlike "credit-card banks", offered by some states, that are more constrained. ILCs can operate in nearly all 50 states by direct mail, charging whatever interest rates they choose.

Amex runs the second-largest ILC, with assets of $17 billion, ahead of the likes of General Electric, Pitney Bowes and BMW. In May, Volkswagen applied to open its own ILC. There are rumours of interest from two giants, Microsoft and Wal-Mart, the kind of threat to prompt a lobbying effort by America's small independent banks to get the loophole closed. Already, Wal-Mart has been stopped from getting a federal savings-bank charter, for fear that the giant retailer might do to local banks what it has done to local stores.

What has grabbed the Federal Reserve's attention is the growing use of ILCs by financial firms, with the result that they escape Fed oversight. Easily the biggest ILC is run by Merrill Lynch, with assets of $54 billion in March, up sharply from $31 billion six months earlier, and less than $1 billion in December 1998. Merrill is now pushing much of the cash held by its stockbroking clients into accounts in its ILC. These pay roughly the same interest rate as the money-market accounts it previously used, but offer the benefit of federal deposit insurance.

Merrill was one of the leading campaigners for the abolition of the Glass-Steagall act that kept investment banks out of commercial banking. Yet, although Glass-Steagall was scrapped last year, Merrill has not formed a bank-holding company, regulated by the Federal Reserve, which the replacement Gramm-Leach-Bliley act allows. Instead, according to Peter Hagan, who runs Merrill Lynch Bank USA, Merrill has quietly become, in effect, the tenth-biggest bank by deposits in America, in large part thanks to its ILC.

Using an ILC is much cheaper than setting up a bank-holding company, Mr Hagan says. He insists that Merrill is simply "executing a strategy that has been in place for four years, before Glass-Steagall was scrapped, which we won't change unless we are forced to." Other investment banks are starting to follow

suit. There is no suggestion that ILCs are shoddily run. But the Fed does not look fondly on the way that some of the world's leading financial firms are getting into banking unscrutinised by its regulators.

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Economics focus

Still broken

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At the Nice summit in December, leaders of the European Union set out to improve the Union's decision-making rules. They seem to have made them worse

THE impending enlargement of the European Union, it is acknowledged, will place heavy demands on the EU's institutional design. A particular worry is that the present system of qualified majority voting (QMV) in the Council of Ministers will become a formula for deadlock once membership expands, as intended, from 15 to 20 and later to 27. The existing QMV rules give big countries extra votes, and then set the threshold for approving a measure at around 70% of the votes cast. Applying this formula as new members join makes it harder to get anything done—because, in effect, the number of possible majorities capable of blocking a given initiative grows faster than the number capable of approving it.

Dealing with this problem was deemed a top priority at the Nice summit, and new rules on QMV were indeed agreed to in the Treaty of Nice. They are due to take effect, subject to the treaty's ratification, in 2005. There is just one problem. The remedy adopted at Nice, far from making deadlock less likely, will leave the Union after enlargement even less able to act than it would have been under the existing rules.

An objective measure of "ability to act" is not an easy thing to produce. But in our economics focus of November 25th last year we described the work of a team of economists who had applied the principles of game theory, and some number-crunching, to the question.

They measured ability to act as the "passage probability" for some randomly chosen initiative—that is, the number of winning coalitions, given the voting rules, divided by the number of all possible coalitions. (The problem is arithmetically demanding. An EU of 15 members has 32,768 possible coalitions; an EU of 27 has 130m.) The absolute value of this probability means little. But *changes* in it are a revealing measure of the extent to which friction has been added or subtracted.

In a new report* for the Centre for Economic Policy Research (CEPR), Richard Baldwin and his colleagues have applied their earlier method to the new treaty. Unreformed, the existing QMV rules give a passage probability of 7.8% for a Union of 15 members; in an EU of 27, again under existing QMV rules, the passage probability falls to 2.5%. With the Nice reforms, the passage probability in an EU of 15 rises, fractionally, to 8.2%; but the reforms actually reduce the passage probability in an EU of 27, to 2.1%.

Compare this with passage probability under the simple dual-majority system favoured by the European Commission (as well as by *The Economist*). If passage had required support from (a) a majority of nations, representing (b) a majority of the EU population, the passage probability would have been 25%, no matter whether the Union had 15 members or 27.

As well as failing to improve the Union's ability to act, the Nice rules make the system far more complicated, and therefore harder to explain to the Union's bewildered citizens. Winning majorities will have to satisfy three criteria: 71% of Council votes (rising to 74% later); a majority of member states; and 62% or more of the EU's population. In addition, the allocation of votes has been tilted further in the direction of the big countries—thus, you might argue, reducing democratic legitimacy from the standpoint of the newcomers. So the EU's leaders have scored three out of three: they have made the system less efficient, more complicated and less legitimate. And people said it couldn't be done.

Show me the money

The European Union has another equally important numbers problem, as Mr Baldwin and his colleagues again point out. Enlarging the Union to add first five and then another seven members threatens to

render unwieldy the policymaking council of the European Central Bank (ECB). At present there are 18 votes on the council: one for each of the 12 central-bank governors and another for each of the six members of the executive board. This is already a big panel. Assuming an EU of 27, with the newcomers all joining the euro, and further assuming that Britain, Denmark and Sweden join too, the council will end up with 33 members.

Not only that, but enlargement will widen the economic differences among countries within the euro area. In particular, many of the newcomers are likely to have higher inflation than the existing members for years to come, because of the so-called Balassa-Samuelson effect. (As productivity and incomes in the poorer countries catch up with those in the rest of the Union, prices of non-traded goods will rise relative to traded ones.)

So the ECB will find its job much harder—just as its ability to do it is being impaired by an overpopulated council. Again, the problem was acknowledged at Nice. In this case, nothing was done: possibly a good thing, in view of the QMV reform. The CEPR team points to three possible solutions. Votes could rotate among council members, Fed-style; groups of countries could be represented by a single voting member; or voting could be delegated to an independent group, such as the executive board. Entrenching the independence of the Bank, which means discouraging decisions on the basis of particular national interests, suggests the third choice, and that is what Mr Baldwin and colleagues recommend.

Despite all of the above, the economists still want to see the treaty ratified. Rightly so, because without it enlargement cannot go ahead, and bringing in the new members ought to be the overriding priority. This does not alter the fact that the EU's "constitution" may now be even more badly broken than it was before Nice. The next, and maybe last, opportunity to fix it will be the inter-governmental conference of 2004.

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* "Nice Try: Should the Treaty of Nice be Ratified?" See www.cepr.org

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The euro

Preparing for take-off

Jun 7th 2001 | FRANKFURT
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The introduction of euro notes and coins brings predictions of disaster

AWKWARD times continue for the European Central Bank (ECB). Although euro-area growth is slowing, inflation is rising and the euro has weakened again. Nobody was surprised when the ECB held interest rates at 4.5% on June 7th. But the ECB has more than monetary policy on its mind. The euro is by far the biggest currency never to have had a physical manifestation. Until now, most of the euro-area's 300m people have had little to do with it, carrying on with D-marks, francs or lire as if nothing had changed; without notes and coins, the euro doesn't seem real. However, on January 1st 2002, euro money is due to arrive. By the end of February, the notes and coins of the area's 12 countries will be gone.

The changeover demands a logistical feat. It has spawned an industry of gosh-did-you-know statistics: in case you care, the total weight of new coins will be 24 times that of the Eiffel Tower. It has also produced apocalyptic warnings of a wave of robberies (think of a till with two lots of cash) and of economic paralysis (shops, on the other hand, may run out of euros). A re-run of the empty millennium-bug scare, perhaps? Or is Europe heading for chaos?

One worry is widespread ignorance about the euro. According to the European Commission, in January 2001 one person in four thought that euros must be issued within one euro-area country to be legal tender there, missing the whole point of a single currency. On average, people thought that national notes and coins would stay in circulation for six months: the right answer is two at most. Conversion from old money to new is not always simple: while Germans can reckon on a bit less than DM2 to the euro, the French have to wrestle with FFr6.56.

Some European parliamentarians have been among the critics of the ECB's plans for distributing euros. Notes and coins will be "front-loaded" to banks. They will pass some on to retailers. Members of the public can buy packs of coins from mid-December. They will not get notes till the new year, from bank machines or counters.

Some say this courts trouble. It would be far better, says a committee of Euro-MPs, to give the public small-denomination notes before January 1st. Shops would then have to hold fewer notes, making them less attractive to robbers. There would be less risk of a shortage of cash in the first few days, and less need to rely on bank machines. People would also have a chance to get used to the new money. That might lead to speedier service in shops, and less confusion and rage: how much change is due from a DM50 note for goods worth *euro*12.16?

Among the direst scenarios, a study for the Dutch national railways reckoned that the queue at Amsterdam's central station on new year's day could run to 1,200 people. In reality, says the report, people would travel without paying. Well, yes. Or they might find something better to do than waiting for a day return to Utrecht.

Other worries also sound overdone. In January, say the commission and the Euro-MPs, "only" 15% knew the exact conversion rates from national currencies to euros. But these are numbers with six significant figures (eg, DM1.95583). Much more encouraging, more than half knew the rate within 1% and almost three-quarters within 5%. The Euro-MPs are also concerned that "only" one person in five has "tried to memorise certain prices in euros". With months still to go, it is surprising that so many have bothered.

The ECB is sanguine. It says, a shade unconvincingly, that giving notes to the public would only confuse

them. Stronger arguments are that the packs of coins will contain *euro*10 or so, more change than most people normally carry; that national notes will still be acceptable; and that a lot of goods and services are paid for with plastic in any case. Information campaigns will build up during the year.

Too sanguine? Until it is too late to make a difference, it is hard to say. But one thing is sure. Success or failure, the euro is unlikely to be greeted with the outpouring of joy that European policymakers think fitting. An opinion poll this week found that Germans would still rather not have the euro at all, and that most expect it to lead to higher prices. A big majority thought that the new money would make European holidays easier. Some advice, then: travel in January, by all means—but don't forget your credit cards.

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Takeovers in Europe

Sugaring the pill

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An unexpected reprieve for Europe's takeover directive

WHEN Vodafone, a British telecoms company, staged a successful *euro*195 billion ($190 billion) hostile takeover of Mannesmann, a German rival, last year, the deal was hailed as a watershed. "Anglo-Saxon capitalism" was to make inroads into the more consensual culture of continental Europe. Combined with the effect of the euro, a wave of mergers was expected, leading to the restructuring of European industry.

The chances of all this happening have been strengthened by an unexpected agreement this week on an EU-wide takeover code, which will make it harder for companies to use "poison pill" defences to ward off takeovers. Such poison-pills—eg, the pre-emptive sale of part of a company, or issuing new shares to friendly parties—will now be legal only if a company's management gets the prior agreement of existing shareholders. This provision should prevent managers putting their own interests ahead of those of shareholders, who might be more willing to sell out.

The takeover directive has been 12 years in the making. It has been opposed by large parts of German industry, and lately by both the German government and German Euro-MPs. They argue that American companies can use various forms of poison-pill defence, and that it is unfair to prevent Europeans from doing the same. Volkswagen, for example, fears that it could become a takeover target as the world car industry consolidates. There has also been opposition from the German chemical industry.

German opposition had been expected to kill the directive. Yet at the last moment, in the early hours of June 6th, a conciliation committee composed of a parliamentary delegation, the commission and the council presidency agreed on a text for the directive. Just as important, from the viewpoint of the pro-takeover lobby, the text made relatively minor concessions to the German position. It agreed only that national governments could now have five years, rather than three, to put the directive into force, and also made it obligatory for hostile bidders to inform workers about potential job losses from restructuring.

Even so, celebrations about the success of the directive could prove premature. It must still get through a vote of the whole parliament in July, as well as being approved by the full Council of Ministers. Euro-MPs are deeply split over the takeover directive. The parliamentary team negotiating with the commission on the directive's text agreed to accept the compromise only after an internal 8-6 vote, with all four Germans against, and all five Britons in favour. The opponents of the directive may now rally support for a last stand. Two years ago an EU directive on biotechnology fell at the last hurdle in a similar situation.

Even if the directive survives July's vote—and the chances are that it will—the hoped-for surge in European takeover activity may take time. The continent's corporate culture is still mostly against hostile bids. And in countries such as Germany and Italy it is common for single shareholders to hold large chunks of big companies, which makes them harder to buy.

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Insuring art

A nice little earner

Jun 7th 2001
From The Economist print edition

Art insurance is a niche market with different rules

AS RISKS go, insurers think of fine art as an attractive one. Transport is the biggest risk, theft the most glamorous. The first can be reduced by expertly packing and shipping sculptures or paintings. The second is limited by the problems in fencing a famous Picasso or Monet. In addition, few connoisseurs think of damaging a work of art—as opposed to, say, their spouse—purely for the insurance claim.

Even so, insuring art has its pitfalls. Insurance losses are rare, but they can be expensive. This is particularly true when an insurance policy is to compensate works at their current market value rather than at a pre-agreed value. The art market has violent swings, but values have largely headed up over the past decade. Two paintings by Turner were stolen in 1994 when on loan in Germany. The claim made to Hiscox, a British insurer, was for £24m ($37m), manageable for a biggish insurer. Three large companies, Hiscox, Chubb in America and Axa Nordstern, a subsidiary of France's Axa that insures only fine art, underwrite the lion's share of insurance policies in the international market, estimated at around $500m in premiums last year.

At present, the art-insurance market is still "soft", insurance-speak for low rates and profitability. But things are looking up. The market for property and casualty (P&C) insurance is recovering, after hitting rock bottom. Fine-art insurance tends to follow general trends in P&C. In particular, says Charles Dupplin at Hiscox, the rates for transit between museums are going up. Transporting works of art across countries and continents is still a risky undertaking. Standards of safety and care vary considerably, say, between America and the former Soviet block.

Who buys art insurance? Museums, auction houses, art dealers and private individuals get cover for their works of art. Auction houses have their in-house insurance policies for art that they sell off. Sotheby's, an auction house, even teamed up with a single brokerage, Marsh & McLennan, to offer insurance to its clients. Museums tend to insure for the largest sums, because of the size of their art collection. But insurers such as Hiscox and Axa Nordstern focus on private clients, because this is where the money is to be made. Rich private collectors buy more than half the policies written by Axa Nordstern, museums only 15%.

Art museums buy less insurance than is widely believed. In many countries they do not get government help to insure their collections, so some do not insure at all; or else they insure only part of their collection. Edvard Munch's "The Scream", for instance, was not insured when it was stolen in 1994 from the National Gallery in Oslo. It was later recovered. National museums in Britain may not buy insurance. They are "self-insured", which means they must settle claims out of already overstretched budgets. In case of theft, a museum could be left with an empty space on its walls, or, put more politely, with a "loss to the nation".

Independent museums in Britain may buy insurance. Yet a report by the Museums and Galleries Commission found that a large proportion are inadequately insured, partly because they are inexperienced in risk management, and partly because of lack of funds.

To help insure, at the very least, loans of art and temporary exhibitions, Britain, America and Australia have put in place an indemnity scheme. The British government insures exhibits from other countries; in some cases loans by British museums to museums abroad; and even loans by national museums to independent museums in Britain. The American government sponsors a programme run by the National Endowment for the Arts that indemnifies (that is, insures) both exhibitions from abroad and exhibitions from America in other countries. The maximum sum for any individual exhibit is $500m, an apparently large sum, but only part of the cover for blockbuster shows these days. Unlike national museums in Britain, which are largely state-funded, American museums can (and do) buy insurance.

In the case of theft or damage, insurers have two main options. A loss adjuster is called in to handle the claim as fairly as possible. And they can make use of databases of stolen art, such as the Art Loss Register in London and the International Foundation for Art Research in New York. Until now, these databases have been only mildly successful in recovering works of art, but they have made dealing in stolen art harder. Enough, says Huntington Block, a pioneer in art insurance, for an art thief to think about a different career.

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Malaysia

Dr Mahathir's one-man show

Jun 7th 2001 | KUALA LUMPUR
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Daim Zainuddin goes as Malaysia's finance minister

ONCE more, Malaysia's prime minister has taken the reins at the finance ministry. In September 1998, Mahathir Mohamad snatched them away from his then deputy prime minister, Anwar Ibrahim, who is now in prison, and slapped capital controls in place to cope with regional turmoil. He eventually handed the job to Daim Zainuddin, a wealthy power-broker and long-time ally who had helped to devise the controls as part of a wider recovery plan. Malaysia's economy outpaced most of its neighbours in 1999 and 2000, defying predictions. Now the economy is back in trouble. And on June 5th Dr Mahathir announced that he would, temporarily, take over the finance job again, following Mr Daim's departure.

This time, however, a sharp change in policy seems unlikely. Whatever his differences with Mr Daim—and rumours of a rift began circulating a year ago—Dr Mahathir has given no hint that he might question parts of Malaysia's macroeconomic game-plan, such as its fixed exchange rate or its effort to prime the fiscal pump. More importantly, although the country's structural policies, and in particular its cosy brand of capitalism, did indeed drive a wedge between the two men, the differences appear to be largely ones of public relations. Several big bail-outs in recent months, of businessmen close to Mr Daim and the ruling party, have drawn ferocious public criticism. But, although Mr Daim's departure will take off some of the heat, it would be surprising if Dr Mahathir followed this up with real reforms.

Start with the macroeconomic problems. A worldwide slowdown has hurt Malaysia more than its neighbours, because of its dependence on exports of electronic goods, especially to America. After expanding by 8.3% last year, GDP grew by only 3.2% in the first quarter, with manufacturing output braking sharply. That will weigh on corporate balance sheets, many of which were never set in order after the region's financial crisis of 1997-98.

Falling regional currencies are also eroding Malaysia's edge. After fixing its exchange rate at 3.80 ringgit to the dollar in September 1998, it gained a competitive boost over its floating neighbours as the region recovered; but now that process has gone into reverse. The government is no longer relying on capital controls to prop up the currency, having removed all but the last barriers only a few weeks ago. But it dismisses any suggestion that it should abandon the fixed exchange rate, arguing that economic stability will outweigh any loss of competitiveness.

Now Malaysia is feeling the tug that dragged down so many fixed currencies before it. After posting impressive gains in 1999 and early 2000, the stockmarket has fallen by 36% over the past 12 months; it has been the worst-performing index in Asia this year. The slide has been driven partly by fears of a devaluation—and if it continues, it could help to make one necessary. A recent report by Deutsche Bank points to the repatriation of profits by multinationals and to private and other capital outflows. Pressure on the currency is likely to increase.

Dr Mahathir's government continues to coddle businesses with historic links to the ruling party, and has done little to encourage firms to use capital more judiciously. Last December, the government paid an associate of Mr Daim twice the market price for his 29% stake in Malaysian Airlines. In February, three government-run funds, including the state's central pension fund, snapped up stakes in TimedotCom, a telecoms firm controlled by another of Mr Daim's associates, after retail investors shunned its public offering. The subsequent losses led even Malaysia's docile trade unions to pipe up.

The bail-outs do not inspire investors, particularly overseas ones, to plunk their money on Malaysia. But

the resulting public outcry has also added political risk to the equation. After two decades in power, Dr Mahathir has said that he will step down before the next elections, due by 2004. Many Malaysians do not believe him, however, and for others it will not be soon enough. Most troubling for Dr Mahathir is the strength of the backlash from members of his own party, the United Malay National Organisation (UMNO). But given UMNO's historic links to so many businesses, things could get even more interesting when Dr Mahathir fills another of the posts that Mr Daim has vacated: party treasurer.

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Planetary formation

A place like home?

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Astronomers studying solar systems have reported a rare find: the very first stirrings of one just like the earth's

SOMETHING is kicking up a lot of dust around Zeta Leporis, a star not unlike the sun that is located 70 light years from earth. According to Christine Chen and Michael Jura of the University of California, Los Angeles, that makes "Zeta Lep", as it is familiarly known, rather special among the small number of stars around which dust has been detected. At a meeting of the American Astronomical Society in Pasadena, California, last week, Dr Chen and Dr Jura said that they saw the dust as evidence that an asteroid belt is forming around the star. That could be a precursor to the formation of rocky planets like Mercury, Venus, Mars—and earth.

Over the past few years about 60 planets have been detected in orbit around stars other than the sun. Such planets, however, are all huge—some, indeed, have many times the mass of Jupiter, the largest planet in the earth's solar system. That is because they are detected by their gravitational effects on the stars they orbit, and only big planets have a strong enough gravity to produce an effect detectable from earth.

These big planets are assumed to be "gas giants" similar to Jupiter and Saturn in composition. The evidence collected by Dr Chen and Dr Jura is the first to show a star in the act of forming a solar system that could contain a rocky, earthlike planet. The finding is made more remarkable by other research presented at the meeting, which suggests it is quite difficult for a star to churn out earthlike planets.

A handful of dust

To make such planets, a star needs solid material—pieces of rock interspersed with iron that can collide and stick together—and not just gas. The rock is formed out of coagulated dust. The dust is formed when suitable molecules cool and combine with each other. These molecules appear at the fringe of the cloud of gas whose gravitational collapse and subsequent heating signals the birth of a star.

That, at least, is the textbook picture, according to John Bally of the University of Colorado at Boulder. What is wrong with it is that the textbooks pretend that the cloud is left undisturbed to do its textbook thing, whereas in reality it is likely to live in an environment that will nip its planetary aspirations in the bud.

Dr Bally showed this by observing star-forming regions in the Orion nebula, and then studying the numbers. Nine of every ten stars that are born from a collapsing cloud, he told the meeting, find themselves next to an extremely luminous "giant" star. The light from such giants blows away the outer gas and dust of their neighbours, leaving nothing to form planets.

Even stars that are born far away from a giant are still likely to be part of a binary or triple star system. Whenever one of these companions passes close by, the pull of gravity causes both stars to send out jets of matter, again wasting the raw material of a possible solar system. According to Dr Bally, unless planetary systems form very quickly after a star is born, they are bound to be rare—occurring around only about 5% of stars. The results of planet-finding programmes so far seem to bear this out.

So it is all the more exciting to see dust of a special kind encircling Zeta Lep. Dr Chen and Dr Jura infer from the infra-red radiation it emits that its temperature is a balmy 70°C. That is so warm it suggests

that the dust is close to Zeta Lep, and is thus being heated by the star. The researchers' calculations place the dust in a ring 2.5 astronomical units from Zeta Lep. An astronomical unit, or AU, is the distance from the sun to the earth, so the position of the dust coincides with that of the rocky planets of the earth's solar system. In all other dust rings found so far—for instance, the much colder ring around the star Beta Pictoris—the distance of the ring from the star is more like 100AU.

The infra-red radiation emitted by the dust can also be used to measure the size of the ring directly, and this has been done using the Keck telescope on Mauna Kea, Hawaii. In visible light, all stars appear as points, only smeared out into a small circle by the atmosphere and by the optics of the telescope. Most stars also look like that when viewed in infra-red light, but for Zeta Lep the circle is bigger than expected. This means that, at that wavelength, it looks like a ball with a radius of 6AU, which agrees pretty well with the value arrived at by Dr Chen and Dr Jura.

Double-checking the dust's distance to the star is crucial, for it is on the basis of this value that the two astronomers build the rest of their conclusions. These start from the observation that, when confronted with starlight, dust orbiting a star does a weird thing. Instead of flying away from the star under pressure from the light, the dust falls towards it.

When confronted with starlight, dust orbiting a star does a weird thing

This is called Poynting-Robertson drag, and it happens because light that hits a dust grain does not bounce off it (which would push the grain away from its parent star), but is absorbed. Once absorbed, it can be re-radiated in any direction. If it is emitted in the direction that the dust particle is travelling, the light waves will be compressed to have a slightly shorter wavelength (this is known as the Doppler effect). The shorter the wavelength, the more energetic the light, which means the particle is ejecting more energy forwards than backwards. That slows it down like a retro-rocket. The result is that its orbit shrinks and it drifts towards the star, which eventually eats it.

Poynting-Robertson drag is a powerful brake. Dr Chen and Dr Jura calculate that, in about 20,000 years, all the dust around Zeta Lep should have fallen into the star. Yet according to accepted models of star formation, Zeta Lep is anywhere between 50m and 400m years old. So, either the astronomers were unbelievably lucky in catching this star during an extremely short phase in its existence, or there must be something replacing the dust.

The most likely source of replacement dust is colliding asteroids. And that suggests Zeta Lep is similar to how the earth's solar system must have looked when it first formed: a ring around the sun in which bits and pieces of rock are constantly bombarded by other bits and pieces of rock, with dust being produced from the collisions.

Dr Chen and Dr Jura have only a vague notion of how large the "parent bodies" of their dust are, but objects a few metres to a few kilometres across—in other words, asteroids—fit the bill nicely. And Mark Sykes, of the Steward Observatory of the University of Arizona, suggested to the meeting that Zeta Lep's nascent solar system could be more complete than that. Asteroids going round a star in nice, circular orbits, he reasons, will not have much cause to collide. If collisions are what is producing the hot dust around Zeta Lep, then the gravity of a large planet must already be stirring things up. That makes Zeta Lep seem even more familiar. Give it another few billion years, and it might look just like home.

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Arctic pollution

POP goes the theory

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The arctic is more polluted than both science and law say it should be

LAST year, scientists discovered that more than 1% of the polar bears on the Arctic island of Svalbard, which belongs to Norway, are hermaphrodites—in other words, they possess both male and female reproductive organs. They attributed the bears' over-endowed condition to PCBs, a group of environmentally persistent industrial chemicals that disrupt animals' hormone systems.

Last month, in Stockholm, 90 countries took a step towards eliminating PCB production when they signed the United Nations Environment Programme's global treaty, banning 12 of the worst persistent organic pollutants (POPs)—a class of toxic chemicals that includes PCBs and many harmful pesticides. Now, researchers have come up with a new reason to put this treaty into effect quickly. According to a study presented on June 1st to the American Geophysical Union, in Boston, the transport of these chemicals to the Arctic may be happening far faster than was previously thought.

Eric Steig, a geochemist at the University of Washington, along with Kathryn Matthews and Mark Hermanson of the University of Pennsylvania, have been looking at PCBs and other POPs, including the notorious DDT, in ice-core samples taken on Svalbard. They found that although many of these pollutants had decreased in concentration since they were banned, the chemicals that were present were fresher than expected. The age of DDT, for example, can be estimated from the ratio of the amount of the chemical itself to the amount of its principal breakdown product, DDE. Some of the pesticide turned out to have been only a few weeks old when it was buried.

That is surprising, because work done in the Canadian Arctic suggests that POPs move north by what is called the "grasshopper effect". This means that they evaporate in warm air and condense when the air cools down. Thus, over the course of several years, they approach the Arctic in a series of seasonal jumps.

The freshness of the POPs in Svalbard suggests that the grasshopper-effect theory is not the whole story, at least in that part of the world. And, while it is possible that conditions in Svalbard are different enough from those in the Canadian Arctic to make this result inapplicable there, preliminary data that Dr Steig has collected in Greenland—which is nearer Canada—appear to agree with the results that he obtained from Svalbard.

What is most worrying is not merely the speed at which pollutants are arriving in the Arctic (which gives them less time to break down before they are preserved in the Arctic ice). The evidence of fresh POPs in the ice cores also suggests that the chemicals are still being used in large quantities. Since most POPs are illegal in most countries, that means somebody, somewhere, is breaking the rules.

Given Svalbard's proximity to Russia, that country is the most likely culprit. No surprise, really, given its environmental track record—but bad news for polar bears who want a normal sex life.

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The scramjet

Whoops!

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AP

The scramjet fails to scram

NASA, America's National Aeronautics and Space Administration, suffered a setback to the aeronautics side of its remit on June 4th. It planned to test the X-43A, a prototype aircraft powered by a supersonic-combustion ramjet, or "scramjet" (see article). The X-43A was designed to travel at seven times the speed of sound. Unfortunately, the scramjet was never even ignited. Its booster rocket went haywire and its controllers blew the whole thing up. Better luck next time.

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Structural genomics

Strategic thinking

Jun 7th 2001
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Biochemists are vying to solve protein structures. They should collaborate

SOLVING the human genome was a doddle. Although it is 3 billion units long, its shape has no bearing on its function. The harder part is to analyse the structure of the proteins that those genes (and the genes of all other creatures) encode. For this, shape matters; and to find the shape of a protein, it has to be purified and either X-rayed to destruction or run through a nuclear-magnetic resonance (NMR) machine. Or you can compare it with a protein whose structure you already know.

That works because proteins come in families that share a common ancestry. Biochemists can thus resort to rough predictions of protein structure based on calculations of family resemblance.

Proteins are composed of amino-acid building blocks, which come in 20 varieties. If two proteins have similar sequences of amino acids, the chances are that they will look similar, too. This is because it is the way that the amino acids in different parts of the sequence interact with one another that determines a protein's shape. A lot of these interactions, though, are with nearby amino acids, and these produce local structures known as domains. Once a known domain is identified in a new protein, that part of its structure can be considered understood. The more domains that are known, therefore, the more scientists can use this short cut to build models of new proteins. The question is: how many different domains must be mapped before biochemists can make accurate predictions about the structure of any new protein, without the need to X-ray or NMR it?

Chris Sander, a researcher at the Massachusetts Institute of Technology, and his colleagues have tried to solve this puzzle. Their goal was to determine how best to go about obtaining a set of experimental data that would allow accurate models to be built for all imaginable proteins.

Since knowing the structure of one member of a protein family lets researchers guess what others will look like, the most efficient strategy for choosing protein targets should cover as wide a diversity as possible. That is not, unfortunately, what is happening. At the moment, laboratories are competing to work out the same protein structures, rather than collaborating in the way that they did to produce the human genome. In this month's *Nature Structural Biology*, Dr Sander and his colleagues put figures on the cost of this unwillingness to work together.

Dr Sander began by assessing how well protein-structure prediction has worked until now. To do this, he surveyed the results of a biennial contest held in Asilomar, California. In this contest, researchers pit their structure-prediction skills against one another. Judging from the winners' models, reliable extrapolations could be made from one protein to another so long as the two shared at least 30% of their amino-acid sequences.

The researchers then set about analysing things at the domain level. They looked at the Pfam database, a repository of the amino-acid sequences of 260,000 protein domains, to find out how easily, using the 30% figure as a guide, these could be clustered into groups that were single units from an analytical standpoint. This would mean that to find the shape of any member of a group, you would need to determine it for only one member. Then, if you found any member of such a group of domains in a protein, you would be able to slot that shape into the overall model of what the protein looked like.

In order to cover all the domains in Pfam, the researchers' software had to create 17,000 groups. Modelling 90% of Pfam, however, required only 4,000—an acceptable trade-off. But the researchers estimate that Pfam's proteins account for only a quarter of the protein families in the genomes that are currently known. Extrapolating from this, they calculate that an optimal strategy for surveying 90% of all protein domains would need 16,000 carefully chosen targets.

Impossible dreams

In practice, marshalling the efforts of laboratories across the world to do that would be an impossible task. The days of happy collaboration over the human genome are gone, not least because a lot of money is now at stake. Proteins are drug targets, and some may become drugs in their own right. The competitiveness of the field means that researchers go to great efforts to conceal the identity of their pet proteins from one another.

Yet this lack of transparency could incur a significant cost. According to Dr Sander and his colleagues, choosing targets at random would mean tackling several times more structures than necessary. Without a co-ordination of effort, the authors conclude, it would require around 50,000 experimental determinations of structure to map out 90% of all proteins. At the current rate of ten structures every week, it would take nearly a century to churn out these data. Of course, technology moves on, and more people may enter the field, so it should not take that long in practice. But a bit of collaboration would speed things up no end.

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Ideas in America

Flexible response

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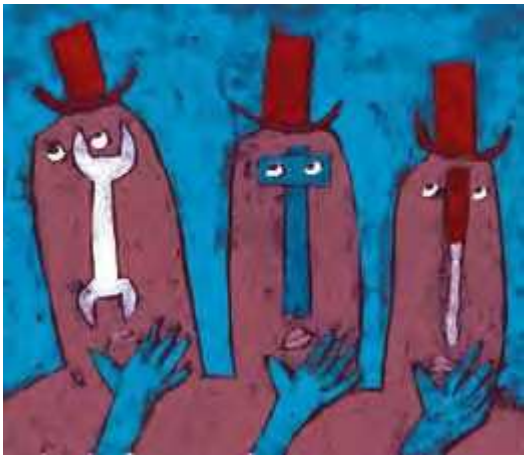
How the pragmatists changed the way Americans thought

The Metaphysical Club
By Louis Menand

Farrar, Straus and Giroux; 558 pages; $27. To be published in Britain in November

Buy it at
Amazon.com
Amazon.co.uk



ABSTRACT argument can get surprisingly out of hand. In the fourth century, before scholastic debate was properly formalised, zealous Christians called Circumcellions roamed north Africa braining theological opponents with cudgels. Despite its menacing sound, the metaphysical club of Louis Menand's title was not a weapon of any kind, but an informal group of young thinkers that met in Cambridge, Massachusetts, in 1872 to address the larger issues of the day, particularly how the demands of law, ethics and religious faith could be reconciled with scientific and technical progress.

Though the club met for less than ten months, it included three men who, in their different ways, left a lasting mark on American thinking in the 70 years between the end of Reconstruction after the civil war and the onset of the cold war after 1945: Oliver Wendell Holmes Jr, William James and Charles Sanders Peirce. Together with John Dewey, a younger member of a milieu to which Peirce gave the name of pragmatist, they form the core of Mr Menand's detailed and fascinating essay on the history of American intellectual life. The sheer range and variety of its material makes the many themes of "The Metaphysical Club" at times hard to follow. But it consistently throws light on a question about America that has so often puzzled outsiders: how does it continue to combine such cold-eyed realism with a boundless, sunny confidence?

The book opens in the shadow of a conflict of principle that left 620,000 American soldiers dead. The frontispiece shows a pencil sketch by James of his brother, Wilky, recovering from wounds that almost killed him which he received while helping lead black troops in a heroic but costly northern assault on Fort Wagner in South Carolina. The text itself starts with the post-war disillusionment of Holmes, an ardent unionist, wounded three times—at Antietam so badly that he was left for dead.

As a brilliant young lawyer in civilian life, Holmes turned his back on the religious enthusiasm and political legalism that, as he saw it, had inflamed passions and clouded reason in the 1840s and 1850s. Whatever he and his generation had gone through before, theirs was now a less innocent, less idealistic and more goal-oriented world. Before long, as America's pre-eminent legal theorist, Holmes developed a theory of law which stressed, not codes or principles, but particular cases and practical results. Here, as applied to law, was the very mainspring of the pragmatists' outlook: the meaning of a doctrine or theory is indistinguishable from the practical effects of adopting it.

James and Peirce were, more strictly, the philosophers of the club, and the pair make a wonderful study in contrasts. James, a natural reconciler, was fluent and sought after. Perhaps his most famous idea—that belief is not ultimately answerable to evidence but to the will—was motivated in part by a wish, in a godly nation, to render faith safe from rational criticism. From his Swedenborgian father he inherited

both a comfortable income and a restless interest in everything human under the sun. He was quick, impatient and unsystematic, faults that made him such a gifted populariser. Though a lifelong depressive, he was both a professional success and an ever-ready help to his younger siblings—including Henry, whom he teased for the long-windedness of his later novels—as well as to his many friends.

Psychology, James's passion and a reason for his popularity, was for Peirce a secondary concern, and in his human relations, this showed. He was a born disturber of the peace. From his astronomer father he acquired a feel for mathematics and physical science; his steadiest job, which he held for 30 years until sacked for misconduct, was at the coastal survey. He was arrogant, hot-tempered and difficult, both in person—a servant sued him for assault—and on the page. A free thinker and philanderer, Peirce scandalised the universities he worked in, started businesses that never went anywhere and ended up begging for charity. Of all the members of the metaphysical club, Peirce's thinking was the most original and, in today's eyes, the most modern: he put statistical reasoning at the centre of scientific method and made serious contributions to semantics and logic. As James's philosophical stock has fallen, so Peirce's has climbed.

Keep it flexible

These are large characters, whom Mr Menand catches well. In expounding particularly their social ideas, he never lets these float far from their context of origin or field of application. The world to the pragmatist is in flux; observation is at best approximate; ideas are tools and all judgment is provisional. Everything on earth, including us and our minds, has evolved, so the best tactic for success is to be adaptable.

It is common enough to observe that "keep it flexible" was a fitting outlook in a can-do young nation, breaking into the world as a new industrial superpower. Bertrand Russell scoffed in 1909 that, if pragmatism held sway, "ironclads and Maxim guns" would become the "arbiters of metaphysical truth". His jibe, though not without logical bite, neglects the democratic thrust of pragmatism, as Mr Menand reminds us: not only codes and categories, but hierarchies and establishments were anathema to it. On the Supreme Court, Holmes advocated free speech and restraints on business power. Dewey's optimistic vision of democracy was all of a part with his progressive views on education, which stressed the needs—and wishes—of the individual child.

Holmes died in 1935, Dewey in 1952. Once they had spread and fructified, the social ideas of the pragmatists came to seem to many Americans naive and old-fashioned. Having started with one war of ideology, Mr Menand ends with two others, in which calculating results gave way again to ideals and principle. For its combat against Soviet communism, America turned from pragmatism, he tells us, to a Protestant realism with a darker view of man and a stricter sense of doctrine. For its second civil war, the fight against segregation in the South, it turned to preachers and dreamers such as Martin Luther King.

Mr Menand offers this story as one approach to the past, not as documented or demonstrable fact. There are many ways to practise the history of ideas, and true to the pluralist tenor of his subject, Mr Menand seems happy to employ almost all of them. You can let ideas unfold in their own space according to their own logic; you can tie every idea back to its social context, to the *Zeitgeist* or to the idea's first known exponent; or you can carry on as if ideas, especially philosophical ideas, have no real history at all—as if the sages of the ages could somehow get together over dinner, as they used to on a TV programme hosted by the late Steve Allen, and chew over timeless conceptual chestnuts. How much real intellectual commerce was there between Mr Menand's chosen four or is the Cambridge club a handy narrative device? If there was such a thing as the spirit of late 19th-century America, did pragmatism express it? Does biography ever illuminate, let alone explain, a thinker's ideas?

Mr Menand, a frequent magazine writer as well as a professor of English, zestfully adopts the contemporary biographical practice of not treating thinkers as disembodied intelligences. In fact, he describes the travails of the scholar's life in such detail that it sometimes seems a miracle they got it down on paper at all. Personal rows, the ups and downs of careers, the snakes and ladders of the academy (Mr Menand is especially good on these) are scrupulously noted. The body's appetites and its frailties are also given full due.

Anybody interested in modern America will find rewards aplenty in "The Metaphysical Club". It enlivens virtually everything it touches, and on its frequent diversions it touches many things: natural selection and racism; probability distributions and disputed wills; the Pullman strike and the turn from laisser-faire; the Dartmouth case and academic freedom. If the rewards are not always where you expect to find

them, that only adds to the stimulation of an urbane and original book. Mr Menand tells a plausible story about the growth and importance of pragmatism in American thought—and he does so without knockdown arguments.

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Architectural styles

Fat or thin

Jun 7th 2001
From The Economist print edition

ARCHITECTS seldom like to think of themselves as subject to anything so trivial as style. It sounds frivolous and arbitrary. For Witold Rybczynski, however, style is the visual language with which architecture expresses itself, a language that is shaped as much by an architect's cultural milieu as by his or her personal taste or talent. We are all inevitably of our time and our look shows it.

The Look of Architecture
By Witold Rybczynski

Oxford University Press; 208 pages; $22 and £14.99

Buy it at
Amazon.com
Amazon.co.uk

Thus, says Mr Rybczynski in these lectures given at the New York Public Library in October 1999, people appreciate architecture, among other reasons, because it prompts them to think who they might have been in the past and how far removed they now may be from that age. A young man dressed in trainers and T-shirt touring Versailles is jarring when he sneaks into the corner of our tourist photo. Were he in period costume, we would feel differently. The same figure in James Stirling's Neue Staatsgalerie in Stuttgart is perfectly in tune with the multiculturalism circulating in that eclectic building.

Such is the visual language of style. Mies van der Rohe's early work in Berlin shouts avant-garde Europe just as the Chrysler Building in New York, which was completed in 1930, is an elegant reminder of the glitzy jazz age of the 1920s and Horace Walpole's 18th-century Thames-side villa evokes the eclectic sophistication of the countrified lifestyle that still stirs nostalgia in many a would-be squire's heart.

Style does not change overnight, but is an accumulation of collective and individual experience. The architect is part of this continuous process of action and reaction in which each generation repudiates the one before to make its mark on the present. The look of that mark depends on the architect's choice of detailing and how he or she relates it to the whole. A stucco or rusticated surface? A metal or wooden railing? Robert Venturi softened his Vanna Venturi House to accommodate his mother's old-fashioned furniture by simply adding moulding. He thus left his particular stylistic mark on this high Modernist building.

Whether it is God or the devil in the details, those details determine the look of things. Quoting from Coco Chanel, Mr Rybczynski's slim volume should help make architects feel more secure: "Fashion passes, style remains".

"Mies in Berlin" is on show at the Museum of Modern Art in New York from June 21st to September 11th before moving to Berlin and then Barcelona. "Mies in America" is on at the Whitney Museum until September 23rd.

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Modern Greek history

From small acorns

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THE violent upheaval which established Greece as a nation state began in 1821, in what is now Romania, when a small force of expatriate Greeks unsuccessfully invaded the Ottoman Empire. In the Peloponnese, armed bands, led by local clergy, attacked their Muslim neighbours, killing the men, enslaving the women and causing an exodus of refugees. The Ottoman government responded by putting to death the Greek patriarch, by terrorising the Greek populations in areas still under its control, and by sending troops to attempt to reassert their authority. In 1825, having lost one army, the Turks encouraged the viceroy of Egypt to send forces to Greece, intending that the Peloponnese, once reconquered, would be resettled with Muslim immigrants from Africa.

The Flame of Freedom: The Greek War of Independence, 1821-1833
By David Brewer

John Murray; 414 pages; £25

Buy it at Amazon.co.uk

From the beginning volunteers from Europe and America, notably Lord Byron, went to Greece to assist the cause, although militarily they made little difference. Two large commercial loans were raised on the London stockmarket which enabled the Greek insurgents to buy arms, including steam-driven warships, and to recruit foreign officers, although these efforts too were largely ineffective. However, just when the Egyptian troops were on the brink of success, the Ottoman fleet was inadvertently destroyed at Navarino in a battle with the British, French and Russians. Since a reconquest then became impossible, the Egyptian troops were withdrawn, and the allies were able to impose a settlement whereby Greece became an independent kingdom under their protection.

David Brewer offers a reliable historical account of these complex events, sketching the characters of the leading participants, attempting to discern strategies and tracing the political shifts within Greece and internationally. He knows the terrain well, writes clearly and is familiar with both Greek and foreign sources. The claim that this is the first book in English for over a century to cover the full story of the war is, however, unfair both to predecessors such as Douglas Dakin and Christopher Woodhouse, who covered many aspects of the war in similar vein in the 1950s and 1960s, and to the careful archival and analytical work of Richard Clogg, Dimitris Livanios and others, who have looked more critically at the inherited narrative which Mr Brewer retells.

Mr Brewer takes care not to disguise the local communal nature of much of the violence nor the readiness of some Greek leaders to make shifting local alliances against their co-religionists and fellow countrymen. Nor does he downplay the massacres, the expulsions and the other examples on both sides of what today would be called ethnic cleansing. However, like Thomas Gordon and George Finlay, who had themselves taken part in the war and from whose sympathetic, exasperated and still highly readable histories Mr Brewer frequently quotes, he presents such episodes as regrettable aberrations in a national liberation struggle. Although as an account of the events of the war, the book can be commended, its explanatory framework is therefore anachronistic and incomplete.

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Contemporary art

Anarchy and ecstasy

Jun 7th 2001 | TURIN
From The Economist print edition

Cornelia Parker's obsession with the past never fails to surprise

EVER since she was a girl growing up on a farm in the north of England, Cornelia Parker has enjoyed getting her hands dirty. In her latest work, "The Sub-conscious of a Monument", she uses dirt excavated from underneath the leaning tower of Pisa to make an earth installation in Turin's Galleria d'Arte Moderna (GAM). "When I learned they were restoring the monument by removing the earth from one side of the tower, I negotiated with the authorities to take some of it because I was fascinated by the idea of taking the sub-soil of such a monument, which hasn't seen the light of day for over 800 years."

Ms Parker loves resurrecting and recycling history, and after the Turin show closes she will take the dirt home to London and process it into other works. Like some mad archaeologist of material culture, Ms Parker sifts through history's leftovers in her own life as well as her art. Her home is a restored print works in London's East End, near the local street markets. "I find walking around Brick Lane far more inspiring in terms of making art than going to a museum," says the artist who has been nominated for the Turner prize and whose work hangs in the Tate Modern. "In a street market the objects still have lots of potential because they are waiting for someone to buy them. Everything's got a history, the narrative never ends."

Ms Parker likes to play with ideas about the monumental, to dig into the dark areas people think they know and to resurrect them into something new and strange and often beautiful:

> "I'm trying to find uncharted territory in the most visited spot or idea, trying to find space where things are the most crowded. It's like going to the eye of the storm. In the shadow of these monuments or icons, there must be the most unstable things in our society, the things that we can't map. And as individuals, we have all that too. There are so many known facts about your life. But really there is this other subtext which is much more interesting, more undiscussable. How do you describe that?"

Ms Parker shot to attention in 1995 with "The Maybe", a coffin-like glass case at London's Serpentine gallery in which an actress, Tilda Swinton, slept during the day, lying in state like a living relic. "The idea of sleeping evoked the idea of life and death, that we're always in this limbo," explains Ms Parker. Ms Swinton was surrounded with relics of famous dead people who had become icons in an earlier age, including Freud, Queen Victoria and Charles Dickens.

Her art often speaks of connections with the past, especially of the contemporary obsession with celebrity and how it confers value on seemingly meaningless objects.

> "I love the power of the relic. Entering an art work is a bit like an act of faith, a transaction between the viewer and the object viewed, and it requires a degree of belief which is entirely personal...I want to make something that's open to projection but I want to do that by using everyday things that we all know, like a dress or a doll. I'm trying to make the world we think we know more porous and less concrete."

Ms Parker often refers to her "very physical upbringing doing repetitive tasks" in the working-class north. She loved working with her hands and went to a local art school because "it seemed like an act of anarchy to do something so apparently useless". Now 45, her anarchy pays the bills: her first solo show toured America to wide acclaim last year and the Victoria and Albert museum has commissioned a major sculpture with which to inaugurate its new British galleries in November.

In the work now on display at the GAM, she has photographed Einstein's lecture blackboards with a microscope, blowing up his chalk scribbles into cosmic visions. In a work called "Shared Fate", she has used the actual guillotine that beheaded Marie Antoinette to decapitate a doll, and credited Madame

Tussaud's Wax Museum in London, where the instrument is part of the chamber of horrors. She has fashioned earplugs out of the dust from the Whispering Gallery in St Paul's Cathedral, calling them "The Negative of Whispers". She paid $5,000 at an auction of celebrity memorabilia for the nightgown from "Rosemary's Baby", Roman Polanski's 1968 horror film, and encased it in a glass vitrine as if it were a holy relic. Obsessed with meteorites—"pieces of space dust"—she buys them on the Internet, then grinds them into a powder of iron ore and blasts them off in fireworks so that they can land again. "I like the idea of a shared fate, of a meteorite that landed in China 500 years ago suddenly falling in our midst." Her next meteorite landing can be seen in Milan later this summer.

When one viewer at the GAM opening asked what this work was all about, she smiled and said: "Life, death and resurrection—we're all experiencing the limbo between life and death. My work is trying to map that in-between space between known and unknown, the constant hovering between two states." This is why she likes to make suspended sculptures. For her signature piece "Cold Dark Matter", one of the most popular exhibits in last year's inaugural hang at Tate Modern, Ms Parker asked the army to blow up a garden shed. She pieced the debris into a spectral constellation suspended in mid-air that seems to freeze-frame the explosion, stopping time in its tracks. Life, in all its past and future.

Cornelia Parker's work can be seen at the Galleria d'Arte Moderna in Turin until June 17th. It will also feature in "Anteprima Bovisa, Milano Europa 2001" in Milan, until September 16th.

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New American fiction

Ageing disgracefully

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PHILIP ROTH fans will remember David Kepesh as the narrator-hero of two earlier novels, “The Breast” (1972) and “The Professor of Desire” (1977). The sex-obsessed pseud is back in “The Dying Animal”. He’s pushing 70 now but his adolescent libido rages on undiminished. Happily for him, as a part-time college lecturer and media pundit, he has no trouble meeting impressionable, pliant young bimbos.

The Dying Animal
By Philip Roth

Houghton Mifflin; 192 pages; $23. Jonathan Cape; £12.99

Buy it at
Amazon.com
Amazon.co.uk

Eight years ago, he tells an unidentified interlocutor as the novel opens, he embarked on an affair with a busty Cuban-American undergraduate called Consuela Castillo. When eventually Consuela dumps her ageing Don Juan, she manages, if not quite to break his heart, at least to bruise it a bit. Still smarting, David relates the course of their affair in lurid detail. This leads him into a breezy disquisition on the delights of the 1960s sexual revolution. (He is especially grateful for the “generation of astonishing fellators” that followed.)

Kenny is the only child of David’s short-lived marriage. He pops up briefly to remind his dad what a rotter he was to abandon both his wife and son once the 1960s started to swing. David merely finds him “ridiculous”. Still, Kenny is at least allowed to air the view that “staying in a difficult marriage and raising a little child and meeting the responsibilities of an adult” might have been a more admirable course of life than rushing around college campuses leaping into bed with every available girl. Finally, Consuela turns up on David’s doorstep to announce that she has breast cancer. This has the effect of a bucket of iced water thrown into his lap: “I couldn’t have slept with her”, he recalls with a predictable measure of sympathy.

As usual with Mr Roth’s books, “The Dying Animal” is fluently written and often very funny. But David is insufferable. He’s not a character that you love to hate. He’s a crashing bore. And, for all his slick patter and casuistry, he has nothing interesting to say about his main themes of sex, death and male-female relations. His typically donnish assessment of the first few times he slept with Consuela might have served as a blurb for the novel as a whole: “controlled by narcissism, by exhibitionism, and despite the energetic display, despite the audacity...strangely inert”.

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Contemporary art

Arte Povera

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From The Economist print edition

Luciano Fabro's “The Mirror of Italy” is just one of the works in a retrospective of the open-ended experimental Arte Povera movement whose anti-aesthetic attitude to art making and materials cleared the ground for so many younger artists working today. Essential viewing for anyone interested in contemporary art, “Zero to Infinity: Arte Povera, 1962-1972” is on show at the Tate Modern in London until August 19th. It then goes on to Minneapolis, Los Angeles and Washington, DC.

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American politics

Bush v Gore, again

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From The Economist print edition

BOOKS IN BRIEF

There is still much to learn from the dead heat of 2000

A SIGN at French level crossings reads, “Un train peut en cacher un autre”—one train can hide another. So with elections, as Douglas Brinkley, a historian, notes in his introduction to this assemblage of *New York Times* reports on the presidential contest. The long battle over the Florida dead heat between George Bush and Al Gore distracted attention from Congress: a 50-50 tie in the Senate and a razor-thin Republican margin in the House, the smallest in half a century. A better instant book would have looked at the 2000 federal elections as a whole. Florida, it is true, was a fascinating political story on any count. But cut and paste is not the best way to retell it.

36 Days
By correspondents of theNew York Times

Times Books; 384 pages; $15

Buy it at
Amazon.com
Amazon.co.uk

THE team from the *Washington Post* offers a sustained and readable narrative. Starting on “the longest day”—the election itself—“Deadlock” takes us through to the night of December 12th when the United States Supreme Court by 5 to 4 terminated the Florida recount, ending Mr Gore’s chances. The teams, the tactics and the might-have-beens are all here. Character sketches and good anecdotes relieve an often tangled story. A succinct chronology also helps.

Deadlock
By the political staff of theWashington Post

PublicAffairs; 272 pages; $23. Plymbridge; £16.99

Buy it at
Amazon.com
Amazon.co.uk

Though an epilogue examines tactical what-ifs, no effort is made to say what it all meant, and the whole story reads rather like an inside view of a tight World Series baseball championship. Obvious questions—Was Mr Gore not trying to overturn a close but clear result? Did Jeb Bush, Florida’s governor, help his brother win? Was the Supreme Court’s final call judicious or partisan?—are met with scrupulous but unilluminating balance. That said, “Deadlock” is easily the best of the instant books on offer.

THIS is, in effect, a long backgrounder to the results of an independent recount of Florida “undervotes”—votes read by machines as showing no mark for president—done for the *Miami Herald.* The results, given in full in an appendix, suggest that, on the generous counting rules the Democrats wanted, Mr Bush would have won by around 1,600 votes—more than his recorded margin of 537; and on the strictest rules, which many Republicans favoured, Mr Gore would have squeaked in by three votes. The report further notes that other disputes and anomalies remain, most of which ought probably to be called in Mr Gore’s favour. The *Miami Herald* is yet to report on its count of “overvotes”, ballots showing two votes for president. There is a map of Florida’s counties and a chapter proposing solutions to vote-counting problems.

The Miami Herald Report
By others and Martin Merzer

St Martin’s Press; 352 pages; $24.95

Buy it at
Amazon.com
Amazon.co.uk

“BUSH v Gore” reprints Supreme Court and Florida opinions but not those of the lower federal courts, as well as op-ed commentaries. The Supreme Court’s tortured final ruling, which has been criticised by legal scholars left and right, deserves rereading—and pondering—in full. So far the best non-specialist discussion, however, is not to be found here but in an exchange in the *New York Review of Books* (January 11th and February 22nd) between two law professors, Ronald Dworkin, a critic, and Charles Fried, a defender of the conservative majority that ruled for Mr Bush. One justice less, and the presidency would have been Mr Gore’s. By an odd symmetry, an unexpected change of one vote has

Bush v Gore: The Court Cases and the Commentary
Edited by William Kristol and E.J. Dionne Jr

Brookings Institution Press; 346 pages; $15.95 and £11.75

now put the Democrats in charge of Senate business, so giving America something closer to the divided government that in 2000, as so often, it seems to have wanted.

Buy it at
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Faisal Husseini

Jun 7th 2001
From The Economist print edition

Faisal Husseini, a Palestinian for coexistence with Israel, died on May 31st, aged 60

AP

"SOONER or later," said Faisal Husseini in an interview last year, "my people will stop listening to clowns like me who preach coexistence and peace." Fundamentalism—Islamic, nationalist and Jewish—was waiting in the wings to take over, and take over it did, in both Palestine and Israel, after the *intifada* broke out towards the end of the year. On June 1st, the day of Mr Husseini's funeral, the omnipresent Israeli police sensibly evacuated themselves from East Jerusalem as tens of thousands of Palestinians saw him off with high honour to his tomb on Haram es Sharif, facing the Dome of the Rock. But that evening, a young Palestinian blew himself up outside a Tel Aviv discotheque, taking 20 Israeli youngsters with him.

The son of a military hero who died defending Jerusalem in 1948, and the grandson of a Jerusalem mayor from the days of the British mandate, Mr Husseini was a princely member of an aristocratic family that has lived in Jerusalem for centuries. A decent, honest man—which is a lot rarer than it should be among the Palestinian glitterati—he inherited the leadership of Palestinians in the city as if by birthright.

Westerners talked of Mr Husseini as a de facto mayor, but perhaps he was more of a *mukhtar*, the head man, an arbiter to whom people turned and whose advice they accepted. Outclassed by Yasser Arafat as a politician, he was an articulate diplomat who spent the last six months of his life travelling in the Palestinian cause, ending up, and dying, in Kuwait, which had not, until he came, let in a senior Palestinian since Mr Arafat put his money on Saddam Hussein in 1991. His official title was the Palestine Liberation Organisation's representative in Jerusalem—the Israelis would not allow Mr Arafat's Palestinian Authority to have a toehold in the city—and he worked from Orient House, a beautiful family-owned former hotel that the Israelis resented, and tried to shut down.

An ardent, pragmatic nationalist

He will be missed, outsiders say, as a Palestinian moderate. But "moderate" is an absurdly over-used term. Mr Husseini abhorred cruelty: days before his death he appeared on Israeli television lamenting the civilian death toll. Beyond this, he was pragmatic in two ways: he believed fervently, and from a fairly early stage, in the two-state, Israeli-Palestinian, solution; and he believed in talking to Israelis, using the fluent Hebrew he had learnt during his five stints in Israeli prisons. He kept in touch with the Israeli peace camp even at a time, during the past few months, when the peace camp itself seemed to have despaired of peace. But he was also an ardent Palestinian nationalist.

He held adamantly to the view that if Palestinian and Israeli states were to coexist peacefully, Israel must agree in principle to withdraw to the border that existed before the 1967 war and Israel's further conquests. He did not accept the 92-95% withdrawals that were bandied about by Bill Clinton and Ehud Barak at the time of Camp David. The Palestinians, he said, should never agree to borders determined by Israeli settlements.

On the other hand, once this was agreed in principle, there could be minor adjustments to allow for some of the Jewish settlements to be included within the Israeli state. These adjustments, he argued, had to be based on negotiation and land swaps, and by swaps he meant exchanges of comparable land, not the chunks of Negev desert that Israel had contemplated offering for good West Bank farmland.

Swapping land could work in Jerusalem too, he argued. His belief that there could be no viable Palestinian state that did not have all of East Jerusalem, including the Old City, as its capital was central.

Jerusalem, he would explain passionately, held the two sections of the West Bank together; it was part of the Palestinian collective memory, every stone had its tale.

He would keep the city united, with the Israeli and Palestinian sectors run by separate municipalities but with many concerns—the environment, sewerage, roads—shared in some sort of higher council. Crucially, he would allow most of the Jewish settlements in East Jerusalem to remain under Israeli sovereignty—in exchange, he argued, for the return of Palestinian-owned land on the borders of West Jerusalem. He pointed out that there was land available for this purpose: for instance, an abandoned Palestinian village north of Bethlehem in West Jerusalem that was still largely unoccupied.

This is not the voice of a moderate, as most Israelis (and many of their American supporters) conceive moderation. But Mr Husseini's answer, if he were called immoderate, would be to say that the Israelis have not, as yet, accepted that peace has its price, and that price is the full withdrawal from the land occupied in 1967.

He was unusually sensitive to Israeli concerns, above all their demographic concern that, at some fairly early point in this half-century, the Palestinians in their territories will match, and then outnumber, the Israeli Jews in theirs. But these fears, he argued, provide excellent reasons for Israel to disgorge Palestinian territory, not to hold on to it, waiting for ever-worse conflict to develop. "The present is my problem," he said at that interview a year ago, looking out over his troubled half-city. "The future is Israel's problem."

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Overview

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From The Economist print edition

There was more encouraging news from the **euro area**. Unemployment fell slightly, from 8.4% in March to 8.3% in April. Producer-price inflation also edged down, from 4.2% in March to 4.1% in April. Only retail sales spoiled the fun; after a disappointing decline of 0.4% in March, volume was up only 1.6% on a year earlier.

Revised figures from **America** showed that labour productivity's rate of change fell to eight-year lows in the first quarter. Rather than dropping by 0.1%, as originally reported, non-farm output per hour sank by 1.2%. Some good news tempered the bad, though: the unemployment rate fell, for the first time in eight months, to 4.4% in May. The markets made steady gains after Alan Greenspan, the Federal Reserve chairman, suggested that stable inflation could pave the way for another cut in interest rates.

Canada's current-account surplus ballooned to US$22.2 billion in the year to the first quarter.

The Nikkei index in **Japan** has lost 9.3% since closing near a six-month high on May 7th. More, and worse, news on the state of Japanese banks' bad loans came out this week.

Sterling fell to a 15-year low against the dollar. The currency lost 1.2% in trade-weighted terms as the Labour Party's gains in pre-election polling raised expectations of an early entry to Europe's monetary union.

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Output, demand and jobs

Jun 7th 2001
From The Economist print edition

% change at annual rate

	GDP		The Economist poll GDP forecasts		Industrial production	Retail sales (volume)	Unemployment % rate	
	1 qtr	1 year	2001	2002	1 year	1 year	latest	year ago
Australia	+ 4.3	+ 2.1 Q1	+ 2.1	+ 3.9	+ 3.1 Q4*	+ 3.0 Q1	6.9 May	6.5
Austria	+ 1.7	+ 2.6 Q4	+ 2.1	+ 2.4	– 5.0 Mar*	– 1.1 Feb	3.7 Apr	3.7
Belgium	+ 1.8	+ 2.4 Q1	+ 2.5	+ 2.6	+ 5.7 Mar*	+ 5.2 Mar	10.2 Apr*	10.5
Britain	+ 1.7	+ 2.6 Q1	+ 2.2	+ 2.7	– 0.8 Apr	+ 5.9 Apr	5.1 Mar‡	5.8
Canada	+ 2.5	+ 2.6 Q1†	+ 2.2	+ 3.1	+ 0.7 Mar	+ 3.0 Mar	7.0 Apr	6.8
Denmark	+ 4.9	+ 1.1 Q4	+ 1.8	+ 2.2	+ 5.2 Mar	– 0.6 Feb	5.4 Mar	5.3
France	+ 2.0	+ 2.7 Q1	+ 2.4	+ 2.5	+ 1.9 Mar	+ 1.9 Mar	8.7 Apr	9.9
Germany	+ 1.5	+ 1.6 Q1	+ 1.6	+ 2.3	+ 1.4 Mar	– 0.6 Mar	9.3 May	9.6
Italy	+ 2.8	+ 2.3 Q1	+ 2.1	+ 2.3	– 0.3 Mar	– 0.2 Mar	9.9 Jan	11.2
Japan	+ 3.0	+ 2.8 Q4	+ 0.5	+ 1.3	– 3.9 Apr	+ 2.1 Mar	4.8 Apr	4.8
Netherlands	+ 0.2	+ 2.0 Q1	+ 2.6	+ 2.9	+ 2.0 Mar	– 3.1 Feb	2.0 Apr§	2.7
Spain	+ 2.9	+ 3.7 Q4	+ 2.8	+ 3.0	– 3.7 Mar	na	13.5 Mar	14.8
Sweden	+ 2.4	+ 2.6 Q4	+ 2.4	+ 2.9	+ 6.2 Mar	+ 2.3 Mar	3.7 Apr*	4.7
Switzerland	+ 7.4	+ 2.5 Q1	+ 1.9	+ 2.1	+ 5.0 Q4*	– 0.6 Feb	1.7 Apr*	2.1
United States	+ 1.3	+ 2.5 Q1	+ 1.6	+ 2.9	– 1.0 Apr	+ 2.5 Apr	4.4 May	4.1
Euro area	+ 2.8	+ 3.0 Q4	+ 2.2	+ 2.5	+ 3.0 Mar	+ 1.6 Mar	8.3 Apr	9.0
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*							
Finland	+ 3.0	+ 5.5 Q4	na	na	+ 0.7 Apr	+ 5.5 Feb	10.3 Apr*	11.0
Greece	na	+ 2.5 2000	na	na	+ 1.9 Dec	+11.8 Jan	na	na
Iceland	na	+ 3.6 2000	na	na	+ 4.2 1999	na	1.3 Jan	1.5
Ireland	na	+11.0 Q3	na	na	+23.0 Mar*	+ 1.6 Mar	3.6 Apr	4.3
Luxembourg	na	+ 8.5 2000	na	na	+ 0.2 Feb*	+ 9.4 Nov	2.6 Mar	2.7
New Zealand	+ 2.2	+ 1.6 Q4	na	na	+ 0.9 Q4*	+ 1.7 Q1	5.4 Q1	6.4
Norway	+ 0.3	+ 1.0 Q4	na	na	– 2.8 Mar	+ 0.8 Mar	3.7 Q1	3.9
Portugal	+ 2.2	+ 3.4 Q4	na	na	+ 6.0 Mar*	– 0.6 Feb	3.8 Q4	4.1

*Not seasonally adjusted. †New series. ‡Jan-Mar; claimant count rate 3.2% in April. §Feb-Apr.

Text refers only to the first 16 countries listed

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Prices and wages

Jun 7th 2001
From The Economist print edition

% change at annual rate

	Consumer prices*			The Economist poll consumer prices forecast		Producer prices*			Wages/earnings		
	1 year		year ago	2001	2002	1 year		year ago	1 year		year ago
Australia	+ 6.0	Q1	+ 2.8	+ 3.6	+ 2.3	+ 5.2	Q1	+ 5.6	+ 5.6	Q1	+ 2.9
Austria	+ 2.9	Apr	+ 1.9	+ 1.9	+ 1.4	+ 3.1	May	+ 2.7	+ 2.5	Mar	+ 2.1
Belgium	+ 3.1	May	+ 2.2	+ 2.1	+ 1.8	+ 3.8	Mar	+ 8.6	+ 1.9	Q1	+ 3.3
Britain	+ 1.8	Apr	+ 3.0	+ 2.0	+ 2.3	+ 0.5	Apr	+ 2.3	+ 5.1	Mar	+ 5.7
Canada	+ 3.6	Apr	+ 2.1	+ 2.4	+ 2.1	+ 2.7	Apr	+ 5.7	+ 1.3	Mar	+ 3.0
Denmark	+ 2.7	Apr	+ 3.1	+ 2.3	+ 2.2	+ 3.6	Apr	+ 5.7	+ 3.8	Q4	+ 4.1
France	+ 1.8	Apr	+ 1.3	+ 1.5	+ 1.5	+ 2.9	Apr	+ 3.5	+ 5.0	Q4	+ 3.4
Germany	+ 3.5	May	+ 1.4	+ 2.3	+ 1.5	+ 4.1	Apr	+ 4.4	+ 1.7	Mar*	+ 2.1
Italy	+ 3.0	May	+ 2.5	+ 2.5	+ 1.9	+ 4.3	Apr	+ 5.4	+ 2.6	Apr*	+ 2.1
Japan	− 0.4	Apr	− 0.8	− 0.4	− 0.3	+ 1.3	Apr	− 0.4	+ 0.2	Apr	+ 2.2
Netherlands	+ 4.9	Apr	+ 2.1	+ 4.0	+ 2.3	+ 5.6	Apr	+ 7.3	+ 3.3	Apr	+ 3.4
Spain	+ 4.0	Apr	+ 3.0	+ 3.3	+ 2.6	+ 2.8	Apr	+ 5.7	+ 2.2	Q4	+ 2.4
Sweden	+ 2.8	Apr	+ 1.1	+ 1.9	+ 1.7	+ 3.3	Apr	+ 3.3	+ 2.1	Mar*	+ 3.4
Switzerland	+ 1.8	May	+ 1.6	+ 1.2	+ 1.2	+ 0.9	Apr	+ 2.8	+ 0.2	1999	+ 0.7
United States	+ 3.3	Apr	+ 3.1	+ 2.9	+ 2.4	+ 3.7	Apr	+ 3.6	+ 4.3	May	+ 3.6
Euro area	+ 2.9	Apr	+ 1.9	+ 2.3	+ 1.7	+ 4.1	Apr	+ 4.7	+ 2.4	Q4	+ 2.3
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 3.0	Apr	+ 2.7	na	na	+ 3.0	Apr	+ 7.1	+ 5.0	Q1*	+ 3.5
Greece	+ 3.5	Apr	+ 2.6	na	na	+ 4.3	Mar	+ 7.9	na		na
Iceland	+ 5.5	May	+ 5.9	na	na	+ 5.7	May	+ 3.6	+ 9.2	Apr	+ 5.3
Ireland	+ 5.6	Apr	+ 4.9	na	na	+ 2.9	Apr	+ 5.4	+ 7.4	Q3*	+ 6.6
Luxembourg	+ 2.8	Apr	+ 2.7	na	na	+ 3.6	Mar	+ 3.2	+ 8.4	Oct*	+ 1.7
New Zealand	+ 3.1	Q1	+ 1.5	na	na	+ 7.8	Q1	+ 4.9	+ 1.8	Q1	+ 1.4
Norway	+ 3.8	Apr	+ 2.6	na	na	+ 9.8	Apr	+ 6.2	+ 4.3	Q4*	+ 4.0
Portugal	+ 4.5	Apr	+ 2.1	na	na	+ 3.2	Apr	+17.7	+ 2.2	Feb*	+ 2.8

*Not seasonally adjusted.

Text refers only to the first 16 countries listed

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Economic forecasts

Jun 7th 2001
From The Economist print edition

Our poll results

Every month *The Economist* surveys a group of economic forecasters and calculates the average of their predictions for economic growth, inflation and current-account balances for 15 countries and for the euro area. The table below also shows the highest and lowest projections for economic growth. The previous month's forecasts, where different, are shown in brackets. The panel has become gloomier about Europe's prospects. German GDP, for instance, is now expected to grow by only 1.6% in 2001, down from a forecast of 1.9% last month and 2.4% three months ago. But the panel has become slightly more optimistic about America, raising its average forecast for GDP growth this year to 1.6%, up from 1.5% a month ago and 1.4% a month earlier. For economic growth in 2002, all but five of the forecasts have been cut.

The Economist poll of forecasters, June averages (previous month's, if changed)

	Real GDP, % change Low/high range		Real GDP, % change average		Consumer prices % increase		Current account % of GDP	
	2001	2002	2001	2002	2001	2002	2001	2002
Australia	1.3/3.1	3.3/5.2	2.1	3.9 (4.0)	3.6	2.3	-2.4(-2.9)	-2.5 (-3.2)
Austria	1.8/2.6	1.6/2.6	2.1 (2.2)	2.4 (2.5)	1.9 (1.8)	1.4	-2.5	-2.4 (-2.0)
Belgium	2.1/3.0	2.0/3.0	2.5 (2.6)	2.6	2.1 (1.9)	1.8 (1.7)	4.1 (4.2)	4.3
Britain	1.9/2.5	2.5/3.3	2.2 (2.3)	2.7 (2.8)	2.0 (1.9)	2.3	-2.0(-2.1)	-2.1 (-2.0)
Canada	1.0/3.2	2.0/3.9	2.2 (2.1)	3.1 (3.2)	2.4 (2.3)	2.1	1.5 (1.2)	1.1 (1.0)
Denmark	1.3/2.4	1.7/3.0	1.8 (1.9)	2.2	2.3 (2.2)	2.2	1.4	1.5 (1.4)
France	2.1/2.8	2.3/3.0	2.4 (2.6)	2.5 (2.7)	1.5 (1.3)	1.5 (1.4)	1.8 (1.6)	1.8 (1.6)
Germany	1.3/2.0	2.0/2.9	1.6 (1.9)	2.3 (2.5)	2.3 (2.0)	1.5 (1.4)	-1.2(-1.4)	-0.9 (-1.1)
Italy	1.7/2.5	1.5/2.6	2.1 (2.2)	2.3 (2.4)	2.5 (2.4)	1.9	-0.3	nil
Japan	-0.5/1.3	0.4/2.7	0.5 (0.6)	1.3	-0.4	-0.3	2.2	2.2
Netherlands	1.9/3.3	2.2/4.0	2.6 (2.8)	2.9	4.0 (3.9)	2.3 (2.2)	3.7 (4.1)	3.8 (4.0)
Spain	2.3/3.3	2.3/3.5	2.8	3.0 (3.1)	3.3 (3.1)	2.6	-2.9	-2.6
Sweden	2.0/3.0	2.2/3.4	2.4 (2.6)	2.9	1.9 (1.7)	1.7	2.2 (2.3)	2.2
Switzerland	1.6/2.5	1.5/2.8	1.9	2.1 (2.2)	1.2	1.2	11.8	11.4
United States	1.0/2.2	1.0/3.7	1.6 (1.5)	2.9 (3.0)	2.9	2.4 (2.3)	-4.2(-4.3)	-4.0
Euro area	1.9/2.5	2.1/2.9	2.2 (2.3)	2.5 (2.6)	2.3 (2.1)	1.7 (1.6)	-0.3	-0.2 (-0.1)

Sources: ABN Amro, Deutsche Bank, EIU, Goldman Sachs, HSBC Securities, KBC Bank, Merrill Lynch, J.P. Morgan, Morgan Stanley Dean Witter, Nordbanken, Decision Economics, Royal Bank of Canada, Salomon Smith Barney, Scotiabank, Shinsei Bank, Warburg Dillon Read.

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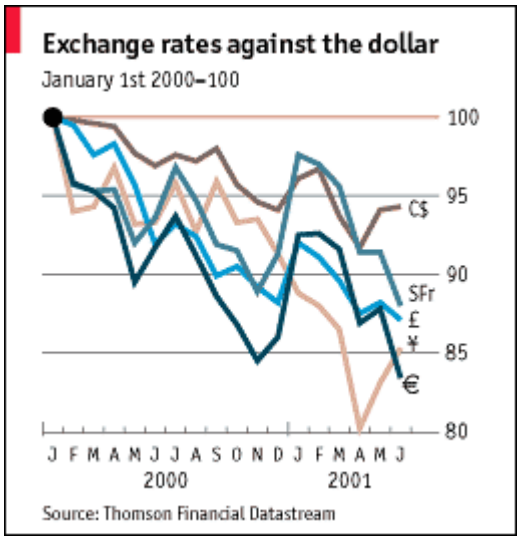
Exchange rates against the dollar

Jun 7th 2001
From The Economist print edition

After staging a recovery at the end of last year, several leading currencies have lost more ground against the dollar. The most beleaguered has been the euro. The yen and the Canadian dollar have begun to rise again.



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The Economist commodity price index

Jun 7th 2001
From The Economist print edition

1995=100

	May 29th	Jun 5th*	% change on one month	% change on one year
Dollar index				
All items	70.4	70.2	– 2.0	– 4.9
Food	67.3	67.4	– 1.6	– 7.4
Industrials				
All	74.6	73.9	– 2.4	– 1.5
Nfa†	73.7	73.1	– 1.7	+ 1.5
Metals	75.4	74.6	– 2.9	– 3.9
Sterling index				
All items	78.3	78.5	– 0.4	+ 2.9
Euro index				
All items	108.4	108.8	+ 2.3	+ 7.6
Yen index				
All items	90.0	89.7	– 3.3	+ 8.5
Gold				
$ per oz	274.55	265.75	+ 0.2	– 8.0
West Texas Intermediate				
$ per barrel	28.83	27.77	+ 0.5	– 7.0

* Provisional. † Non-food agriculturals.

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Stockmarkets

Jun 7th 2001
From The Economist print edition

Market indices

	Jun 6th	2001 high	2001 low	% change on one week	% change on record high	% change on Dec 31st 2000 in local currency	% change on Dec 31st 2000 in $ terms
Australia (All Ordinaries)	3,355.2	3,370.7	3,094.3	+ 0.5	– 0.5	+ 6.4	– 1.7
Austria (ATX)	1,235.9	1,237.4	1,052.2	+ 4.4	–28.9	+15.1	+ 3.9
Belgium (Bel 20)	2,896.9	3,030.4	2,591.6	+ 3.0	–21.3	– 4.2	–13.6
Britain (FTSE 100)	5,901.5	6,334.5	5,314.8	+ 1.8	–14.8	– 5.2	–11.5
Canada (Toronto Composite)	8,194.4	9,348.4	7,415.5	+ 1.1	–28.0	– 8.3	– 9.8
Denmark (Copenhagen SE)	922.2	1,002.1	818.3	+ 0.6	–11.2	+ 1.7	– 8.2
France (SBF 250)	3,532.2	3,820.2	3,107.9	+ 0.6	–19.6	– 6.3	–15.5
(CAC 40)	5,496.5	5,998.5	4,824.8	+ 1.0	–20.6	– 7.3	–16.3
Germany (Xetra DAX)	6,192.4	6,795.1	5,388.0	+ 2.5	–23.2	– 3.7	–13.2
Italy (BCI)	1,697.1	1,948.4	1,609.6	– 1.3	–22.2	–11.4	–20.1
Japan (Nikkei 225)	13,174.8	14,529.4	11,819.7	– 2.4	–66.1	– 4.4	– 9.4
(Topix)	1,307.5	1,441.0	1,162.0	– 1.7	–54.7	+ 1.9	– 3.4
Netherlands (AEX)	590.0	642.3	518.3	+ 1.3	–15.9	– 7.5	–16.5
Spain (Madrid SE)	916.7	963.9	818.6	+ 1.0	–20.0	+ 4.1	– 6.1
Sweden (Affarsvarlden Gen)	253.2	292.7	217.2	+ 1.0	–36.7	– 8.7	–21.0
Switzerland (Swiss Market)	7,581.4	8,135.4	6,574.0	+ 0.3	– 9.9	– 6.8	–15.9
United States (DJIA)	11,070.2	11,337.9	9,389.5	+ 1.8	– 5.6	+ 2.6	+ 2.6
(S&P 500)	1,270.0	1,373.7	1,103.3	+ 1.8	–16.9	– 3.8	– 3.8
(Nasdaq Comp)	2,217.7	2,859.2	1,638.8	+ 6.4	–56.1	–10.2	–10.2
Europe (FTSE Eurotop 300) *	1,457.6	1,545.5	1,279.0	+ 0.9	–14.5	– 4.9	–14.3
Euro area (FTSE Ebloc 100) *	1,306.7	1,404.1	1,143.9	+ 1.2	–15.7	– 6.1	–15.3
World (MSCI) †	1,128.3	1,249.2	1,014.6	+ 0.8	–22.0	na	– 7.5
World bond market (Salomon) ‡	427.7	447.8	426.2	+ 0.3	– 6.8	na	– 3.5

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms.
‡Salomon Smith Barney World Government Bond Index, total return, in dollar terms.

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Trade, exchange rates and budgets

Jun 7th 2001
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current account $bn latest 12 mths		The Economist poll % of GDP, forecast 2001	2002	Exchange rate trade-weighted† Jun 6th	year ago	Currency units per $ Jun 6th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2001‡
Australia	− 2.6	Apr	− 12.9	Q1	− 2.4	− 2.5	72.5	76.1	1.95	1.70	2.71	1.65	1.62	0.1
Austria	− 5.1	Feb	− 4.2	Mar	− 2.5	− 2.4	99.6	100.3	16.3	14.4	22.6	13.8	13.5	-0.6
Belgium	+ 12.8	Mar	+ 11.6	Dec	+ 4.1	+ 4.3	98.0	99.2	47.6	42.2	66.4	40.3	39.6	0.7
Britain	− 44.3	Mar	− 24.5	Q4	− 2.0	− 2.1	106.6	104.8	0.72	0.66	–	0.61	0.60	1.2
Canada	+ 40.4	Mar	+ 22.2	Q1	+ 1.5	+ 1.1	79.1	80.0	1.53	1.48	2.13	1.29	1.27	2.6
Denmark	+ 5.9	Mar	+ 3.7	Mar	+ 1.4	+ 1.5	100.9	101.0	8.81	7.80	12.3	7.46	7.31	2.9
France	+ 0.9	Mar	+ 25.0	Feb	+ 1.8	+ 1.8	100.5	102.0	7.75	6.86	10.8	6.56	6.43	-0.5
Germany	+ 54.4	Mar	− 25.7	Mar	− 1.2	− 0.9	97.2	98.8	2.31	2.04	3.22	1.96	1.92	-1.7
Italy	+ 1.6	Mar	− 5.6	Feb	− 0.3	nil	71.7	72.8	2,287	2,023	3,187	1,936	1,899	-1.3
Japan	+ 98.9	Apr	+110.5	Mar	+ 2.2	+ 2.2	142.9	154.7	120	106	168	102	–	-6.3
Netherlands	+ 16.5	Mar	+ 16.0	Q1	+ 3.7	+ 3.8	96.8	98.1	2.60	2.30	3.63	2.20	2.16	1.3
Spain	− 39.1	Mar	− 17.3	Feb	− 2.9	− 2.6	73.5	74.3	196	174	274	166	163	nil
Sweden	+ 11.0	Mar	+ 5.5	Mar	+ 2.2	+ 2.2	74.6	84.6	10.91	8.70	15.2	9.24	9.06	3.6
Switzerland	− 0.4	Apr	+ 31.1	Q4	+11.8	+11.4	107.1	105.1	1.80	1.64	2.50	1.52	1.49	na
United States	−454.6	Mar	−434.9	Q4	− 4.2	− 4.0	120.4	108.9	–	–	1.39	0.85	0.83	2.1
Euro area	− 4.5	Mar	− 32.6	Mar	− 0.3	− 0.2	76.2	80.3	1.18	1.05	1.65	–	0.98	-0.6
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 13.3	Mar	+ 9.7	Mar	na	na	77.2	77.3	6.73	6.21	9.38	5.70	5.59	5.3
Greece	− 7.5	Q4	− 8.1	Dec	na	na	56.9	58.2	385	351	537	326	320	nil
Iceland	− 0.4	Apr	− 0.9	Q4	na	na	na	na	97.1	75.2	135	82.2	80.6	2.4
Ireland	+ 27.1	Feb	− 0.7	Q4	na	na	86.7	88.0	1.12	0.82	1.56	0.95	0.93	4.5
Luxembourg	− 2.4	Jan	+ 1.6	Q4	na	na	98.0	99.2	45.6	42.2	63.6	38.6	37.9	3.6
New Zealand	− 0.3	Apr	− 2.7	Q4	na	na	79.5	82.4	2.36	2.12	3.29	2.00	1.96	1.0
Norway	+ 27.5	Apr	+ 24.9	Mar	na	na	95.3	91.2	9.11	8.65	12.7	7.71	7.56	15.3
Portugal	− 12.4	Feb	− 10.1	Mar	na	na	88.6	89.4	227	209	316	192	188	-1.2

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †1990=100. Bank of England. ‡OECD estimate.

Text refers only to the first 16 countries listed

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Money and interest rates

Jun 7th 2001
From The Economist print edition

	Money supply* % change on year ago			Interest rates % p.a. (Jun 6th 2001)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+13.5	+ 7.0	Apr	4.95	6.17	5.34	6.00	6.12	7.34
Britain	+ 7.7	+ 7.9	Apr	5.16	6.13	5.18	5.05	5.11	6.69
Canada	+11.4	+ 4.8	Apr	4.30	5.55	4.80	5.71	5.92	7.36
Denmark	+ 1.5	– 3.5	Apr	5.00	4.77	4.77	5.27	5.56	7.20
Japan	+ 6.0	+ 2.7	Apr	0.01	0.03	0.04	1.22	1.71	1.36‡
Sweden	+ 5.8	– 0.3	Apr	4.03	3.93	4.49	5.23	5.00	5.36
Switzerland	– 2.2	+ 2.4	Apr	3.15	3.11	3.10	3.43	3.89	4.09
United States	– 0.1	+10.4	Apr	3.94	6.58	4.09	5.25	6.12	7.03
Euro area†	+ 1.8	+ 5.2	Apr	4.45	4.65	4.26	4.97	5.05	5.59

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds.‡ New series. Benchmarks: US 30-year 5.65%, Japan No.231 1.26%. Central bank rates: US fed funds 4.00%, ECB refinancing 4.50%, BOJ overnight call 0.01%, BOE repo 5.25%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, OM Fixed Income Exchange, Warburg Dillon Read, WEFA Group, Westpac, Thomson Financial Datastream. Rates cannot be construed as banks' offers.

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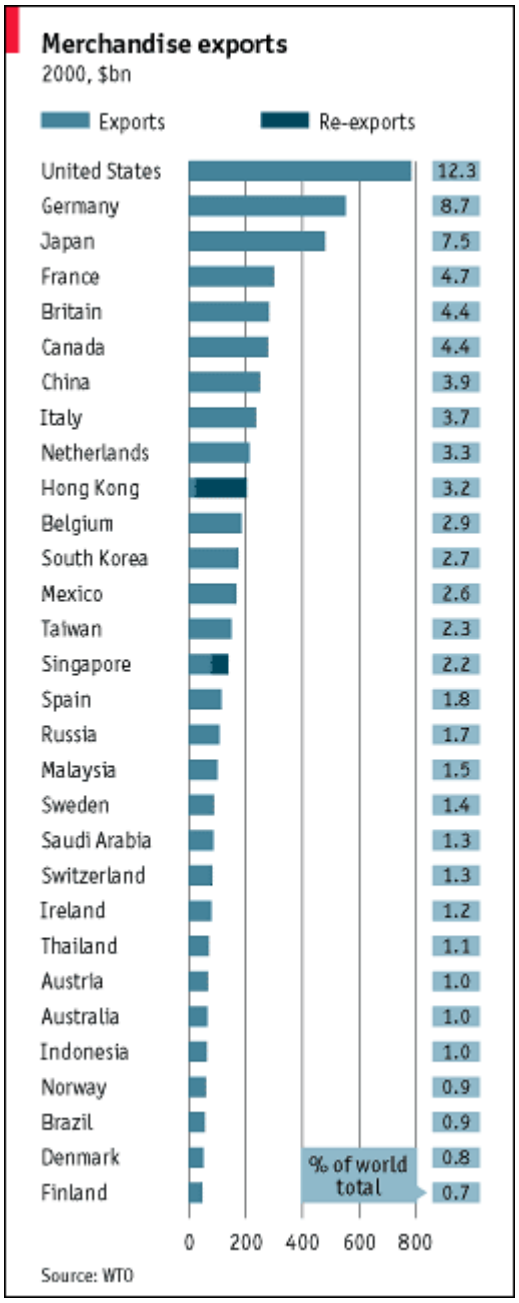
Merchandise exports

Jun 7th 2001
From The Economist print edition

With exports of goods accounting for 3.9% of the world's total, China has a case for making the "quad" of big traders (America, the EU, Japan and Canada) into a "quint" once it joins the World Trade Organisation.



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Financial markets

Jun 7th 2001
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Jun 6th		Dec 31st 2000	
	Jun 6th	year ago	Jun 6th	% p.a.		one week	in local currency	in $ terms
China	8.28	8.28	11.5	na	2,328.3	+1.3	+6.2	+6.2
Hong Kong	7.80	7.79	10.9	3.78	13,576.0	+1.2	-10.1	-10.1
India	47.0	44.7	65.5	7.37	3,457.3	-5.6	-13.0	-13.5
Indonesia	11,195	8,635	15,604	16.53	397.6	-2.8	-4.5	-17.5
Malaysia	3.80	3.80	5.30	3.30	564.1	-1.2	-17.0	-17.0
Philippines	50.7	42.4	70.7	10.25	1,389.5	-0.5	-7.0	-8.4
Singapore	1.81	1.72	2.53	2.25	1,679.1	+1.0	-12.9	-16.7
South Korea	1,286	1,113	1,792	5.78*	597.7	-4.9	+18.4	+16.5
Taiwan	34.1	30.7	47.5	4.10	5,220.4	+3.2	+10.0	+6.9
Thailand	45.3	38.9	63.1	3.50	310.5	+0.1	+15.3	+10.5
Argentina	1.00	1.00	1.39	9.38	439.2	+2.6	+5.3	+5.2
Brazil	2.38	1.81	3.32	16.81	15,328.8	+5.8	-1.7	-19.5
Chile	607	525	846	3.64**	5,435.6	+0.3	+11.6	+5.6
Colombia	2,303	2,126	3,210	12.73	872.0	-0.5	+22.3	+18.8
Mexico	9.12	9.81	12.7	10.39	6,791.0	+3.1	+20.1	+26.5
Peru	3.55	3.49	4.9	12.88	1,408.8	+7.3	+16.6	+15.8
Venezuela	715	679	997	14.96	7,715.9	-1.7	+13.6	+11.1
Egypt	3.87	3.46	5.40	9.08	6,238.9	-5.8	-18.6	-18.2
Israel	4.14	4.15	5.77	5.09	417.1	+0.0	-15.7	-17.7
South Africa	8.09	6.97	11.3	10.59	9,332.9	-0.3	+12.1	+4.9
Turkey	1,170,000	610,765	1,630,746	59.00	11,733.1	+9.8	+24.3	-28.8
Czech Republic	40.3	37.8	56.1	5.07	426.5	-1.5	-10.9	-16.7
Hungary	296	271	412	11.13	6,993.4	-0.2	-10.9	-14.9
Poland	4.00	4.34	5.58	17.08	15,244.9	-1.6	-14.6	-11.8
Russia	29.2	28.3	40.7	25.00	213.4†	+3.8	+51.7	+48.9
EMF (MSCI)‡	1.00	1.00	1.39	na	330.7	-0.6	na	-1.4
EMBI+§	1.00	1.00	1.39	na	215.9	+2.7	na	+6.5

*Last week's rate. **Inflation adjusted. †In dollar terms. ‡Emerging Markets Free. §J.P. Morgan Chase's Emerging Markets Bond Index Plus.

Sources: National statistics offices, central banks and stock exchanges; Thomson Financial Datastream; EIU; Reuters; Warburg Dillon Read; J.P Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; *Russian Economic Trends*.

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Economy

Jun 7th 2001
From The Economist print edition

	% change on year earlier						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 8.1	Q1	+11.5	Apr	+ 1.6	Apr	+22.3	Apr	+20.5	2000	178.0	Feb
Hong Kong	+ 2.5	Q1	– 0.2	Q4	– 1.4	Apr	–11.9	Apr	+ 8.8	Q4	115.1	Apr
India	+ 6.0	Q2	+ 1.3	Mar	+ 2.3	Apr	– 5.7	Apr	– 5.4	Q4	39.9	Apr
Indonesia	+ 4.0	Q1	+ 4.5	Q4	+10.8	May	+26.1	Apr	+ 5.5	Q3	22.1	Apr
Malaysia	+ 3.2	Q1	– 0.3	Apr	+ 1.6	Apr	+15.6	Apr	+ 8.4	Q4	26.8	Mar
Philippines	+ 2.5	Q1	– 2.0	Mar	+ 6.5	May	+ 7.3	Mar	+ 9.4	Jan	12.8	Mar
Singapore	+ 4.5	Q1	– 0.8	Apr	+ 2.0	Apr	+ 4.2	Apr	+21.8	Q1	77.6	Mar
South Korea	+ 3.7	Q1	+ 5.7	Apr	+ 5.4	May	+15.0	May	+14.0	Apr	93.4	May
Taiwan	+ 1.1	Q1	– 5.9	Apr	– 0.2	May	+10.6	Apr	+12.0	Q1	110.6	Mar
Thailand	+ 3.1	Q4	– 1.8	Mar	+ 2.8	May	+ 3.1	Apr	+ 6.9	Apr	31.5	Apr
Argentina	– 2.6	Q4	+ 8.6	Apr	– 0.2	Apr	+ 1.5	Mar	– 9.4	Q4	20.5	Apr
Brazil	+ 3.8	Q1	+ 6.1	Apr	+ 7.1	Apr	– 1.8	May	–26.6	Apr	34.1	Mar
Chile	+ 3.3	Q1	+ 3.1	Apr	+ 3.7	May	+ 1.5	Apr	– 1.4	Q1	14.3	Apr
Colombia	+ 1.8	Q1	+ 3.0	Mar	+ 7.9	May	+ 0.6	Mar	– 0.1	Q4	9.7	Apr
Mexico	+ 1.9	Q1	– 1.9	Mar	+ 7.1	Apr	– 9.5	Apr	–17.8	Q1	40.3	Apr
Peru	– 0.9	Apr	– 6.3	Mar	+ 2.6	May	– 0.4	Mar	– 1.7	Q4	8.2	Mar
Venezuela	+ 3.5	Q1	na		+12.6	May	+17.5	Nov	+12.5	Q1	11.5	Apr
Egypt	+ 6.5	2000†	+ 9.4	2000†	+ 2.4	Mar	–10.4	Q4	– 0.8	Q4	12.9	Feb
Israel	+ 3.0	Q4	– 1.0	Mar	+ 1.2	Apr	– 7.5	Apr	– 0.7	Q3	23.5	Apr
South Africa	+ 2.7	Q1	+ 1.8	Mar	+ 6.5	Apr	+ 3.7	Apr	– 0.5	Q4	6.2	Mar
Turkey	+ 8.3	Q4	– 7.6	Mar	+52.4	May	–26.3	Mar	– 8.1	Mar	18.5	Apr
Czech Republic	+ 3.9	Q4	+ 9.8	Mar	+ 4.6	Apr	– 3.6	Apr	– 2.7	Q1	13.0	Apr
Hungary	+ 4.4	Q1	+ 9.7	Apr	+10.3	Apr	– 2.4	Apr	– 1.7	Apr	11.3	Apr
Poland	+ 2.4	Q4	+ 3.6	Apr	+ 6.6	Apr	–10.0	Apr	– 8.8	Apr	27.1	Mar
Russia	+ 6.8	Q4	+ 5.2	Apr	+25.0	May	+60.7	Mar	+45.9	Q1	25.9	Mar
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Pakistan	+ 3.9	1999†	+ 7.9	Oct	+ 4.2	Mar	– 1.7	Apr	– 2.5	1999	1.2	Apr
Saudi Arabia	– 0.8	1999	na		– 0.2	Mar	+24.9	1999	+ 0.4	1999	16.9	Mar

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Text refers only to the first 25 countries listed

Sources: National statistics offices, central banks and stock exchanges; Thomson Financial Datastream; EIU; Reuters; Warburg Dillon Read; J.P Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; *Russian Economic Trends*.

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Overview

Jun 7th 2001
From The Economist print edition

In the 12 months to May, **Brazil**'s trade deficit widened to $1.8 billion, as outbreaks of foot-and-mouth disease curtailed its beef exports. The country's industrial production rose by 6.1% in the year to April, down from 7.7% in the year to March.

Year-on-year economic growth in the **Philippines** slowed to 2.5% in the first quarter, the smallest rise for two years. This coincided with a slower 12-month growth in consumer prices; inflation fell to 6.5% in May.

Inflation in **Turkey** accelerated to 52.4% in May. That figure was better than expected, however, and the country's stockmarket gained 9.8%.

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